A TREATISE

ON THE

LAW OF PRIVATE CORPORATIONS

BY

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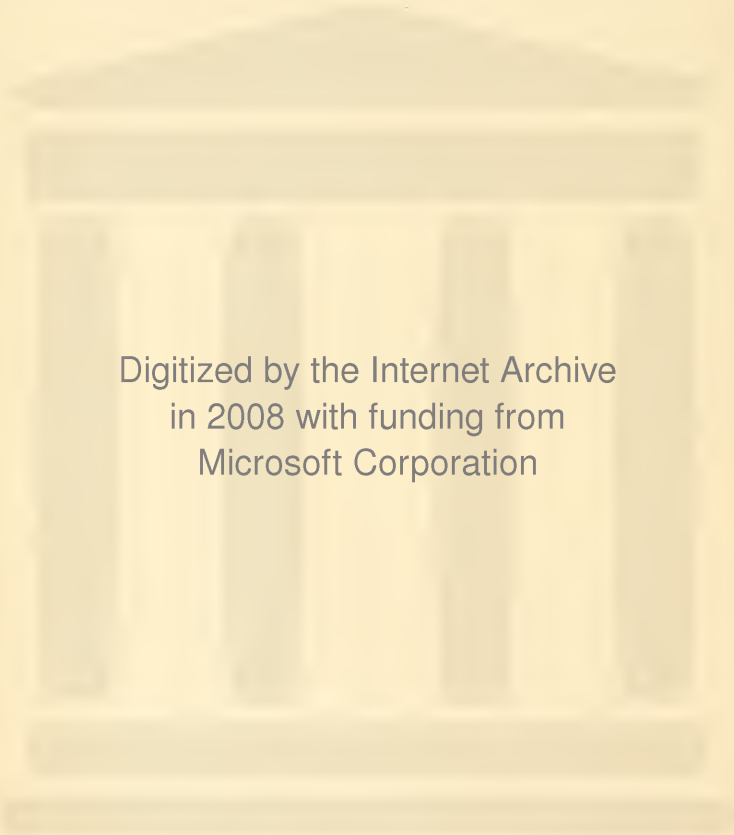

This book has been thoroughly revised and rewritten, and the author trusts that in its present form it will be of value to the student, the teacher of law. and the lawyer engaged in the active practice of the profession.

Minneapolis, November, 1899.

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THE

LAW OF PRIVATE CORPORATIONS

CHAPTER 1.

DEFINITION AND CLASSIFICATION.

§ 1. Introductory.
2. Definition.
3. Origin and growth of corporations.
4. Organization and powers.
5. Corporations during the Middle Ages.
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20. Joint stock companies.

§ 1. **Introductory.**—Every civilized state has found it necessary to confer certain powers and privileges upon juristic persons formed by the aggregation of natural persons. These legal persons are invested with rights and privileges apart from the rights and privileges of the natural persons which form their constituent parts, and are by the law endowed with certain attributes not possessed by natural persons, such as continuous existence. These creatures of the law are called corporations, and that branch of the law of the land which defines and regulates the application of the general law to these juristic persons is called the law of corporations.

§ 2. **Definition.**—A corporation is defined as "an artificial person, created by law, or under authority of law, from a group or succession of natural persons, and having a continuous existence irrespective of that of its members, and powers and liabilities different from those of its members."[1]

This is a very satisfactory definition of a modern corporation, but it is doubtful whether the description given by the earliest writer upon the subject can be improved upon. A corporation, says Kyd, is a "collection of many individuals united into one body under a special denomination, having perpetual succession under an artificial form, and vested by the policy of the law with the capacity of acting in several respects as an individual, particularly of taking and granting property, of contracting obligations and of suing and being sued, of enjoying privileges and immunities in common, and of exercising a variety of political rights more or less extensive according to the design of its institution, or the powers conferred upon it either at the time of its creation or any subsequent period of its existence."[2]

[1] The Century Dictionary. (Austin Abbott.) As to meaning of "continuous existence" and "perpetual succession," see State v. Hannibal, etc., R. Co., 138 Mo. 332, 36 L. R. A. 457.

[2] Kyd I, 13. See State v. Standard Oil Co., 49 Ohio St. 137, 30 N. E. Rep. 279. The celebrated definition of Chief Justice Marshall in Dartmouth College v. Woodward, 4 Wheat. 518, 636, is as follows: "A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly, or as incidental to its very existence. These are such as are supposed best calculated to effect the object for which it was created. Among the most important are immortality, and, if the expression may be allowed, individuality; properties by which a perpetual succession of many persons are considered as the same and may act as a single individual." For other definitions see Minor, Inst. I, 541; Taylor, §§ 1–9; Potter I, ch. 1; Waterman I, § 1; Thomas v. Dakin, 22 Wend. 9; Southern Pac. R. Co. v. Orton, 32 Fed. Rep. 457; Baltimore R. Co. v. Fifth Baptist Church, 108 U. S. 317; Railway Co. v. Allerton, 18 Wall. 233; Tippling v. Pexall, 2 Bulst. 233; People v. Assessors, 1 Hill (N.Y.) 620. In In re Gibbs Estate, 157 Pa. St. 59, 22 L. R. A. 276, the court said: "A corporation is an artificial person created by law as the representative of those persons, natural or artificial, who contribute to, or become holders of shares in, the property intrusted to it for a common purpose. As it is the creature of positive law, its rights, powers and duties are prescribed by the law. Beyond the legitimate purpose which it was created to serve, and the lines of limitation the law has drawn around it, it is without power to act or capacity to take." See Andrews Bros. v. Youngstown Coke Co., 86 Fed. Rep. 585.

Whether an aggregation of individuals is a corporation is determined rather by the faculties and powers conferred than the name or description given it.[1]

§ 3. **Origin and growth of corporations.**—A recent writer has said that the Romans made the world over again, but that among their many achievements none was more durable in its effect on the civilization of mankind than the invention of corporations as an instrument of government and trade.[2] The Roman mind was early familiar with the idea of a number of individuals grouped into a unit.[3] But the conception of a juristic person does not seem to have been fully developed until the latter portion of the time of the Republic. But corporations under various names were common from very early times and are expressly recognized in the Twelve Tables.[4] Prior to about the end of the Republic these associations seem to have been recognized not as persons, but as aggregations with some of the rights of persons. Gradually, however, the idea developed until the entire body of corporations was brought within the realm of private law. As said by Sohm:[5] "Roman law contrived to accomplish a veritable masterpiece of juristic ingenuity in discovering the notion of a juristic person; in clearly grasping and distinguishing from its members the collective whole as the ideal unity of the members bound together by a corporate constitution; in raising the whole to the rank of a person and in securing it a place in private law as an independent subject of proprietary capacity standing on the same footing as other private persons."

The history of corporations in Rome shows the usual fluctuations of opinion with reference to their value to society. At times they were encouraged, and members of the patrician element, under the convenient cloak afforded by their organization, were enabled to engage in trade, from which its members were other-

[1] Edgeworth v. Wood, 58 N. J. L. 463, Wilgus' Cases. See § 31, *infra*.

[2] Baldwin, Modern Political Institutions, p. 141; Bl. Com. I, 468; 1 Minor's Inst. 500; 1 Kent Com. 525, note; 1 Kent Com. 268.

[3] Niebuhr, Hist. of Rome, I, p. 340.

[4] See generally Mommsen's Hist. of Rome, Vol. II, 68; Vol. IV, 267; Vol. V, 370, 373. See Table viii, 1 Kent Com. 524, note.

[5] Institutes of Roman Law, p. 106. See Wilgus' Cases.

wise debarred by law or public sentiment.[1] In the time of the Republic the formation of voluntary corporations seems to have been unrestricted, but they increased so rapidly that they became unpopular, and by a law of 64 B. C. they were all dissolved. But a few years later the charters were revived and their scope much extended. Under Julius Cæsar each charter had to be submitted to him for approval, and the objects of the corporation therein clearly defined.[2] Although corporations existed and seem to have been the subject of private law, Justinian makes no reference to them in the Institutes; but they are mentioned in several places in his digest.[3]

§ 4. **Organization and powers.**—These juristic persons were created for the various purposes of government, the control of colleges and hospitals and the pursuits of commerce. They were created by a law, a decree of the senate or an imperial constitution.[4] They could be formed by three persons but continued by one, and had continuous succession during the period provided by law for their existence, without reference to the changes in the management. Their powers and privileges varied according to their constitutions, but generally they had authority to sue and be sued, choose officers to manage their business, elect new members from time to time, and make by-laws consistent with their constitution and the laws of the land.[5] The title to their property was vested in the juristic person and not in its members, and the members were not individually liable for the debts of the corporation. There is a difference of opinion as to the majority required to transact the business.[6] The corporation existed so long as the es-

[1] Niebuhr, Hist. of Rome, I, 447; Mommsen, Hist. of Rome, B. III, ch. 12. Cato not only took shares in a trading corporation, but loaned it money and sent his agent Quintus to look after his investment. See Plutarch, Life of Cato (Clough's Tr.), II, pp. 344, 345.

[2] Mommsen, Hist. of Rome, Book V, ch. 11; Hunter's Roman Law, 314.

[3] See Taylor Corp., ch. 1, and note in Wilgus' Cases.

[4] Savigny, System des Heutigen Römischen Rechts, §§ 85–102.

[5] Gaius, Elements of Roman Law (Poste's Trans.), 143, 144.

[6] See Rattigan: The Roman Law of Persons, p. 200. The rule seems to have been that a majority of at least two-thirds of the voting members should be present and that a majority of such should agree in order to render a resolution obligatory upon all. But opinions differ.

sential conditions required for its existence continued. But if the state withdrew its sanction the corporation was at an end. Those organized for purely private purposes are said to have ceased to exist when the last member died, although Savigny says that this did not occur in the case of corporations of a permanent character designed for public purposes. Some writers assert that the corporations could be dissolved by a resolution of a majority of the members, although jurists like Savigny and Puchta claim that the consent of the state was necessary to the dissolution as well as the creation of a corporation.[1] When a public corporation which was specially endowed by the state was dissolved, its property reverted to the state. And the same result followed in the case of other corporations, when there was no heir who could take the property.[2]

A corporation could not be guilty of a crime, as it could not entertain the necessary intent. Justinian says that "There is no theft without the intention to commit theft," and it was held that "penal enactments are applicable only to beings capable of feeling, thinking, and exercising the power of volition."[3] In addition to the ordinary corporation aggregate, the Roman law recognized a special kind of corporate body, which resembled the corporation sole of the English law. It included (1) The State; (2) the Prince, in so far as he was the representative of sovereign power; (3) every public officer considered with reference to the rights and duties attaching to the office; (4) the Fisc, or public treasury; and (5) the *hereditas jacens*, the inheritance of a deceased person so long as it is not taken up by any one as heir. These were all regarded as juristic persons, possessed of rights as such.[4]

[1] Rattigan, p. 202.

[2] Mackeldey, Mod. Civ. Law, I, 148.

[3] Gouldsmit's Pandects, § 34, note.

[4] Mackenzie, Roman Law, p. 163.

The general rights of corporations in respect of ownership, possession, obligations and actions were, in Justinian's time, the same as those of natural persons except where the absence of the facts of family life and of the peculiar incidents of humanity (as birth, death, and marriage) destroyed the analogy between artificial and natural persons. With this exception, the difference between the rights and duties of corporations and those of natural persons were the following:

(1) In respect of *usufruct*, or the

§ 5. **Corporations during the Middle Ages.**—After the fall of Rome the commercial corporations disappeared, and only those survived which were connected with the church. Certain organizations in the form of guilds of workmen, which had been known from very early times, now gained great strength. In 1582, Henry III of France authorized the organization of workmen in the several cities, and in the eighteenth century the entire trade of the city of Paris was in the hands of six great, and forty-four lesser, corporations. These incorporations possessed special privileges and were sometimes outside of the jurisdiction of the ordinary courts. Their powers increased until they constituted in each city an *imperium in imperio*.[1] They controlled all the offices, and obtained the sanction of the government to whatever they thought for their own benefit. The guild hall was the city hall. But as the spirit of popular liberty increased, these exclusive, restrictive organizations gradually lost their power, until they were practically all destroyed by the French Revolution and the reform legislation which followed that period.

§ 6. **The great trading corporations.**—The tendency during this period was to concentrate political power in the cities, and the feudal kings sought to neutralize it by chartering great business corporations for adventure and foreign trade. The Hanseatic Leagues of the Middle Ages were in a certain sense

rights of using and taking the fruits of what was owned by another, the duration of such a right was limited to one hundred years.

(2) In the case of a township (*civitas*) making a contract of loan, in which an equal quantity of things of the same kind and value is to be returned to the lender (*mutuum*), the township is only bound so far as the loan is really to its advantage.

(3) A corporation could not be sued for fraud, but its individual directors could, and its corporate acts might be set aside on the ground of undue pressure exercised by it.

(4) Certain corporations had specially granted to them the right to succeed on an intestacy and in priority to the public treasury, to the property of their deceased members.

(5) The rights of corporations to enter on an inheritance as *heir*, to take a legacy, and to benefit from a trust under a will (*fideicommissum*), were all generally recognized in Justinian's time, but it was only by gradual legislative efforts in imperial times that this had been fully brought about. Amos Prin. of Civil Law, p. 120.

[1] See, generally, Gross, The Gild Merchant, London, 1890; Merlin, Répertoire de Jur., VI, 446, *et seq.*; Motley, The Dutch Republic, I, 36.

commercial partnerships, which sought political strength in order to force commercial privileges. These trading corporations gradually obtained control of all the territory which was then being exploited. They were of two classes, one in which membership was obtained by the payment of a fee, and each member traded for himself at his own risk and upon his own capital. The other kind had a common stock, and the trading was by the corporation, under the management and for the benefit of all the stockholders.[1] In 1216 or 1248 the first of these trading companies was authorized in Burgundy by the Duke of Brabant, under the name of the Brotherhood of St. Thomas à Becket of Canterbury. A century later it was transferred to England and its privileges confirmed by Edward III and later by Henry VII, who changed its name to the Merchant Adventurers of London. These great monopolies, without whose permission no one could trade, increased until, by the close of the reign of Elizabeth, they had gathered five-sixths of the foreign trade of England into the port of London and into the hands of two hundred shareholders.[2] But the world gradually grew larger and many companies were organized for its exploitation. The East Indian Company was chartered under Elizabeth, and the Hudson Bay Company in 1670. The Russian Company, the Eastland Company and the Levant Company were organized about the same time. English colonies in America were planted by corporations operating under similar charters. The promoters of the Plymouth Colony were known as the Merchant Adventurers, and had a capital stock of seven thousand pounds.[3] The Dutch East India Company began the first settlement on Manhattan Island, and a similar Swedish corporation established a settlement in Delaware. The Richelieu chartered the Company of New France and gave it title to almost the whole of Canada.[4] Many similar corporations were organized about this time, and their exclusive privileges made them the

[1] Smith, Wealth of Nations, iii, B.V., ch. 1, p. 108. See article on Chartered Companies, in 3 Enc. of the Law of England, p. 148.

[2] Gross, The Gild Merchant, I, p. 148; Hume's Hist. of Eng., Vol. II, p. 284.

[3] Palfrey, Hist. of New Eng., I, 153, 216, 221.

[4] Baldwin, Mod. Polit. Inst., p. 168.

subject of hatred among the people.[1] Many proved disastrous failures, but a few, like the Hudson Bay Company, prospered exceedingly and retained their charters until comparatively recent times.[2]

§ 7. **Early incorporation in the United States.**—Corporations were sometimes created during the colonial period. In some cases the charters were granted by the governor as the representative of the crown and occasionally by the crown itself.[3] Several of the older colleges were incorporated by the colonial legislatures. In 1637 Massachusetts chartered the artillery company which is still in existence. In 1732 Connecticut chartered a company for trading purposes, with power to "encourage the fishery, etc.," which, by virtue of the "etc." grant, immediately established a bank. This, however, was treated as an usurpation, and the corporation lost its charter.[4] About the same time numerous corporations were organized in

[1] Daniel Defoe, in his Essay on Projects, says: "Here begins the forming of public joint-stocks which, together with the East India, African, and Hudson Bay Companies, before established, begot a new trade, which we call by a new name, stockjobbing, which was at first only the simple occasional transferring of interest and shares from one to another as persons alienated their estates; but by the industry of the exchange brokers, who got the business into their own hands, it became a trade, and one, perhaps, managed with the greatest intrigue, artifice and trick that ever anything that appeared with a face of honesty could be handled with. Thus stockjobbing * * * and projecting * * * indeed are now almost grown scandalous."

For the history of the South Sea Company see Mahon's Hist. of England, I, ch. xi; Blanqui's Hist. Polit. Econ., ch. xxxi. For speculative and gambling insurance companies, Smith, Wealth of Nations, iii, 122.

[2] The Hudson Bay Company continued in business until 1867, when its exclusive rights were purchased by the government. Winsor, Crit. and Nar. Hist. of Am., VIII, p. 60.

The company attempted at one time to do a life insurance business. See Child v. Hudson Bay Co., 2 Peere Williams 207 (1723).

[3] Denton v. Jackson, 2 John. Ch. 320; Wilson's Works, Vol. II, p. 561; 3 Bland's Ch. 416, note, Wilgus' Cases.

[4] Colonial Records of Conn., VII, p. 390. This suggests the way in which the Manhattan Bank secured its charter. There being no chance of obtaining a charter for banking purposes, Aaron Burr secured a charter for a company to supply the city of New York with water, with authority to use its surplus capital "in any way not inconsistent with the laws and constitution of the United States in the state of New York" This was in 1799 and the bank is still doing business under the charter. Parton's Life of Burr, 238. The Century Magazine, May, 1899.

the colonies for the purpose of issuing paper money, but in 1720 an act of Parliament prohibited such incorporation.[1] In 1748 the Ohio Company obtained a charter directly from parliament. No charters were granted in Maryland prior to the Revolution.[2] The constitutional convention refused to grant the power to create corporations to the federal congress, but immediately after it went into effect they were created under the implied power. During this early period the practice of incorporation was looked upon with disfavor[3] and charters were very difficult to obtain and were therefore very valuable. But a change of opinion has gradually taken place until the present policy is free incorporation.[4]

§ 8. **The juristic person.**[5]—The idea of separate personality is at the base of the concept corporation. A juristic person can not exist without the capacity for rights and liabilities distinct from those of its members. The rights of a corporation are not the joint rights of the sum of its individual members, but the sole rights of the collective whole of its members. This collective whole or invisible entity which is called into existence and lives by means of the corporate constitution, and which operates not through the medium of other persons, but immediately, is a new subject of rights and duties. It is a community viewed as the subject of rights. The sharp line of demarkation between the collective person and the separate

[1] See Sumner's History of American Currency, 28.

[2] McKim v. Odom, 3 Bland's Ch. 418. See a History of the Law of Private Corporation before 1800, by Prof. Williston, 2 Harv. Law Rev. 105, 149.

[3] In 1733 Lord Bathurst wrote to Swift: "All corporations of men are perpetually doing injustice to individuals. I will attend it, but am as much prejudiced against them as possible, though I know nothing of the man nor the matter in question. I have often reflected (from what cause it arises I know not) that though the majority of a society are honest men, and would act separately with some humanity, and according to the rules of morality, yet, conjunctively, they are hard-hearted, determined villains." Swift's Works, Nichols' ed., XII, 452; quoted in Baldwin Mod. Pol. Inst. 193. See also 2 Hume's Hist. of England, ch. 26, p. 256; Smith's Wealth of Nations, iii, B. V., ch. 1, p. 145.

[4] For the development of the practice of free incorporation, see "Freedom of Incorporation," Baldwin, Mod. Pol. Inst.; 2 Kent Com., p. 268 and note.

[5] See note, Wilgus' Cases, Corporation as a person.

members expressed the fundamental idea underlying the Roman law of corporations. German mediæval law never got beyond the idea that the rights of a corporation were the joint rights of its members. But the English common law fully recognized the separate personality of the corporate entity.[1] It inherited this principle from the Roman law, and adorned it with such metaphysical conceptions as "invisibility," "intangibility," "immortality," and "soullessness." Coke, who was almost the embodiment of the common law, says that "A body politic is a body to take in succession formed (as to that capacity) by policy, and therefore it is called by Littleton a body politic; and it is called a corporation or a body incorporate *because it is made into a body*, and of a capacity to take and grant." The distinction between the rights of a corporation and the rights of its members is well illustrated by the rule of the Roman law that a slave could not be tortured for the purpose of extorting information to be used against his master. But the slave of a corporation could by torture be compelled to give information against the members of the corporation. He was the property of the juristic person, the *corpus*, and not of its members. So, by the common law, the title to the corporate property is in the juristic person, and can be conveyed only in the corporate name, although one person may be the holder of all the capital stock.[2] An action of replevin or for the conversion[3] of the property of the corporation

[1] For the history of "fictitious persons" in the common law, see Pollock and Maitland, History of English Law, I, pp. 469, *et seq.*; Wilgus' Cases, note, Corporation as a person.

[2] In Rough v. Breitung (Mich.), 75 N. W. Rep. 147, it was said: "Stockholders do not own the corporate property and can not mortgage, sell or convey it. The title is in the artificial being called the corporation, not in the stockholders. Such property is not under the control of its stockholders, whether they act separately or collectively. The laws under which these corporations are organized provide the agencies and methods by which their property can be sold and transferred." England v. Dearborn, 141 Mass. 590; Smith v. Hurd, 12 Metc. (Mass.) 371; Moore, etc., Co. v. Towers, etc., Co., 87 Ala. 206, 13 Am. St. R. 23, 6 So. Rep. 41; Parker v. Bethel, etc., Co., 96 Tenn. 252, 31 L. R. A. 706; Button v. Hoffman, 61 Wis. 20, 20 N.W. Rep. 667, 50 Am. Rep. 131; Barrick v. Gifford, 47 Ohio St. 180, 21 Am. St. R. 798; Wheelock v. Moulton, 15 Vt. 519; Humphrey v. McKissock, 140 U. S. 304; Baldwin v. Canfield, 26 Minn. 43.

[3] Tomlinson v. Bricklayers' Union, 87 Ind. 307.

can not be brought by a stockholder, nor can the stockholders bind the corporation by their contract.[1] The declarations or admissions of stockholders as such are not admissible in evidence against the corporation;[2] nor are the stockholders parties to an action against the corporation,[3] although for certain purposes a judgment against a corporation is conclusive against its stockholders.[4] As a corporation is a distinct personality in the eye of the law, it may sue or be sued by,[5] or convey or receive a conveyance from, a stockholder.[6]

The citizenship of a corporation may be different from that of its stockholders. Thus, a vessel which belonged to a British corporation was held entitled to British registry, although certain of the stockholders were foreigners.[7] In a suit against a corporation the stockholders can not set off their individual claims against the claim of the plaintiff, although the plaintiff is insolvent. In a case where this was attempted,[8] Mr. Justice Mitchell said: "In dealing with the right of creditors, and the obligations existing between a corporation and its shareholders, by reason of their contract of membership, undoubtedly the courts often find it necessary to consider the real parties in interest as the individual shareholders; but it may be laid down as a rule, that except in such cases it has been found absolutely essential for the administration of justice to treat a corporation as a collective entity, without reference to its individual shareholders."

[1] Davis v. Creamery Co., 48 Neb. 471, 67 N. W. Rep. 436; Moore H. H. Co. v. T. H. Co., 87 Ala. 206, 6 So. Rep. 41, 13 Am. St. 23; Sellers v. Greer, 172 Ill. 549, 40 L. R. A. 589, Wilgus' Cases.

[2] Polleys v. Ins. Co., 14 Me. 141.

[3] Merchants' Bank v. Cook, 4 Pick. 405. In Mercantile Nat. Bank v. Parsons, 54 Minn. 56, it was contended that notice to certain stockholders was notice to the corporation. The court said: "Generally, and for most purposes, a corporation is a legal entity, distinct from the body of its stockholders and, in any event, to render the knowledge of the individual corporators the knowledge of the corporation it must be the knowledge of all the corporators."

[4] See Hale v. Hardon, 95 Fed. Rep. 747 (C. C. A., May 31, 1899) and cases cited; Mutual, etc., Co. v. Phœnix, etc., Co., 108 Mich. 170, 62 Am. St. R. 693, Wilgus' Cases.

[5] Rogers v. Society, 19 Vt. 187.

[6] Foster v. Comrs., etc., 1 Q. B. 516; Pope v. Brandon, 2 Stew. (Ala.) 401.

[7] Queen v. Arnaud, 16 L. J. N. S. C. L. 50.

[8] Gallagher v. Germania, etc., Co., 53 Minn. 214.

§ 9. **The fiction theory.**[1]—Some modern decisions show a disposition to disregard the principle that a corporation is a person separate and distinct from the individuals who compose its membership. Thus, where the corporation sought to escape responsibility for certain contracts by having them made with the individual stockholders instead of in the corporate name, the court said that it would look beneath the surface and recognize the fact that these individuals were in fact the corporation. But this merely goes to the question whether the state will permit that to be done indirectly which can not be done directly. So the departure from the original idea of no personal liability on the part of a stockholder which has been effected by legislation is not inconsistent with the principle that the corporation is a juristic person. This liability is from the individual member to the creditor, and the corporation is only indirectly, if at all, affected by it.

The statement is generally made by American and English jurists and courts that the corporation is an artificial person, or a fictitious entity.[2] This theory has been strongly assailed in recent times by German jurists, who insist that the distinctiveness of the corporate personality is as real as the individuality of a physical person.[3] Instead of being a mere figure of speech, the legal person created by the law is a reality. The fiction theory undoubtedly prevails in this country, and is the prolific cause of much unsatisfactory reasoning. It has been much criticised within recent years, but upon grounds which are inconsistent with the acceptance of the organic theory. If the corporation is a mere fiction, a figment of the imagination, it is easy to "look beneath it" or disregard it when it is in the way; but a fact can not be so easily disposed of. Few decisions, however, are the results of careful reasoning upon a clearly accepted and recognized theory. Modern courts are, to a great extent, concerned with the rights and liabilities of mem-

[1] See Wilgus' Cases, note. The corporation as a collection of individuals.

[2] Holland's Jurisprudence, 8th ed., p. 82; Markby's Elem. of Law, §§ 161, 136; Definitions quoted, § 2, *supra*.

[3] Holzendorff's Rechtslexikon, Art. Juristische Person, by Prof. Gierke. See for a full and satisfactory discussion Freund's The Real Nature of Corporations, Univ. of Chicago Studies in Political Science, 1897.

bers of corporations having capital stock; and when it is necessary to determine individual rights or to preserve state control over a corporation, they will not permit a theory to prevent a decision which justice and public policy require.

§ 10. **Illustrations.**—As stated in the preceding section, it is held in certain recent cases that when an attempt is made to use the theory of corporate personality for ends subversive of its reason, the courts will treat the corporation as a mere collection of individuals. Hence, under some circumstances, the acts of all the stockholders may be treated as the acts of the corporation and result in bringing upon it the penalty of dissolution. In *quo warranto* proceedings brought against a corporation by the state to deprive it of its franchise on the ground that it had abused its privileges by becoming a party to an illegal trust agreement, the corporation denied that it entered into the contract, but it appeared that the contract was signed by all the shareholders. It was contended that the agreements were the agreements of the individual shareholders in their individual capacities, and with reference to their individual properties, and hence not corporate agreements. But the court held that the acts of the stockholders under the circumstances, were the acts of the corporation and said:[1]

"The idea that a corporation may be a separate entity, in the sense that it can act independently of the natural persons composing it, or abstain from acting, where it is their will that it shall, has no foundation in reason or authority, is contrary to the fact, and to base an argument upon it, where the question is as to whether a certain act was the act of the corporation or of its stockholders, can not be decisive of the question, and is therefore illogical; for it may as likely lead to a false as to a true result. So long as a proper use is made of the fiction that a corporation is an entity apart from its shareholders, it is harmless, and, because convenient, should not

[1]State v. Standard, etc., Co., 49 Ohio St. 137; see People v. North River, etc., Co., 121 N. Y. 582, 24 N. E. Rep. 834; Woodbridge v. Pratt & Whitney Co., 69 Conn. 304; Andrews Bros. v. Youngstown Coke Co., 86 Fed. Rep. 585.

be called in question; but where it is urged to an end subversive of its policy, or such is the issue, the fiction must be ignored, and the question determined whether the act in question, though done by shareholders—that is to say, by the persons united in one body—was done simply as individuals, and with respect to their individual interests as shareholders, or was done ostensibly as such, but, as a matter of fact, to control the corporation, and affect the transaction of its business, in the same manner as if the act had been clothed with all the formalities of a corporate act. * * * Applying, then, the principle that a corporation is simply an association of natural persons, united in one body under a special denomination, and vested by the policy of the law with the capacity of acting in several respects as an individual, and disregarding the mere fiction of a separate legal entity, since to regard it in an inquiry like the one before us would be subversive of the purpose for which it was invented, is there, upon an analysis of the agreement, room for doubt that the act of all the stockholders, officers, and directors of the company in signing it should be imputed to them as an act done in their capacity as a corporation? * * * Where all, or a majority, of the stockholders comprising a corporation do an act which is designed to affect the property and business of the company, and which, through the control their numbers give them over the selection and conduct of the corporate agencies, does affect the property and business of the company, in the same manner as if it had been a formal resolution of its board of directors, and the act so done is *ultra vires* of the corporation and against public policy, and was done by them in their individual capacity for the purpose of concealing their real purpose and object, the act should be regarded as the act of the corporation; and to prevent the abuse of corporate power, may be challenged as such by the state in a proceeding in *quo warranto*."

§ 11. **Kinds of corporations.**[1]—Corporations are classified according to their form, nature and the purpose of their crea-

[1] See Wilgus' Cases Corps.

tion. The principal kinds are designated as public, private, aggregate, sole, ecclesiastical, lay, civil and charitable.[1]

§ 12. **Public corporations.**—To this class belong such corporations as are created for purposes of government and the management of public affairs. They are involuntary, and there is no contractual relation existing between the members or between the corporation and the state. They are simply political agencies created by the state for governmental purposes, but they are sometimes granted corporate or private powers to be exercised for the benefit of the persons who constitute their members.[2]

§ 13. **Municipal and public quasi-corporations.**—Excluding from consideration the class of corporations sometimes called *quasi*-public corporations, that is, corporations which partake both of the nature of public and private, we divide public corporations proper into municipal corporations and public *quasi*-corporations. The former are complete corporations, with all the powers, duties and liabilities incident to the *status*, such as cities, towns and villages. The latter possess but a portion of the powers, duties and liabilities of corporations and include counties, townships, town supervisors, road districts and school districts.[3]

§ 14. **Quasi-public corporations.**—The term *quasi*-public corporation is often used to designate a corporation properly classed as private, but which is engaged in a business of such a nature that the public has an interest therein, as grain elevators, railway, telegraph, telephone, gas and water companies. The private property which is devoted to such purposes becomes "affected with a public interest and ceases to be *juris privati* only," and may be controlled by the public for

[1] In an article on the classification of corporations, in IV Yale Law Journal 97, Judge Oliver P. Shiras suggests a division into political, public and private.

[2] For authorities, see Dillon Munic. Corp., I, § 19; Elliott Pub. Corp., § 2; McKim v. Odom, 3 Bland's Ch. 407, Wilgus' Cases.

[3] Talbott Co. v. Queen Anne Co., 50 Md. 245; Hamilton County v. Mighels, 7 Ohio St. 110, Wilgus' Cases.

the public good to the extent of the interest thus created.[1] But it is a misnomer to call such corporations *quasi*-public corporations; a railway may be a *quasi*-public highway, but the corporation is private.[2]

A boom company is said to be a *quasi*-public corporation intended to supply facilities to the general public for the driving of logs.[3]

§ 15. **Private corporation.**—A private corporation is an incorporated association formed by the voluntary agreement of its members, having for its object the advancement of the private interests of the members. It is sometimes difficult to determine whether a corporation is public or private, but the simple and sufficient test is found in the purpose of its creation. If it is an agency for the administration of government it is public, but if its primary purpose is the private emolument of its members it is private, although the state may hold a part or even all of its shares of stock.[4] The true criterion is whether the objects, uses and purposes for which the corporation was organized are solely for the public benefit and convenience, or for private emolument, and whether the public can participate in them by right or only by permission. The mere fact that a corporation is subject to visitation and inspection by a public official does not make it a public corporation.[5]

§ 16. **Corporations, aggregate and sole.**—A corporation which is composed of several persons is called a corporation

[1] Munn v. Illinois, 94 U. S. 113; Railroad Commission Cases, 116 U. S. 307; Hockett v. State, 105 Ind. 250; Spring Valley Water-works v. Schottler, 110 U. S. 347; Miners' Ditch Co. v. Zellerbach, 37 Cal. 543, 99 Am. Dec. 300.

[2] Pierce v. Commonwealth, 104 Pa. St. 150; Wolffe v. Underwood, 96 Ala. 329, 8 S. Rep. 774. But see State v. Carr, 111 Ind. 335; United States v. Joint Traffic Assn., 171 U. S. 505, 570; Smyth v. Ames, 169 U. S. 466; United States v. Freight Assn., 166 U. S. 290, 332. A corporation organized to conduct a race-track and offer purses is a private corporation, and may refuse to allow certain persons to enter horses. Corrigan v. Coney Island Jockey Club (N. Y.), 2 Misc. Rep. 512.

[3] West Branch Boom Co. v. Lumber, etc., Co., 121 Pa. St. 143, 6 Am. St. R. 766.

[4] Regents v. Williams, 9 Gill & J. (Md.) 232; Bank of U. S. v. Planter's Bank, 9 Wheat. 904, Wilgus' Cases.

[5] Wisconsin, etc., Co. v. Milwaukee Co., 95 Wis. 153, 36 L. R. A. 55; Bank v. Gibbs, 3 McCord (S. C.) 377, Wilgus' Cases.

aggregate,[1] while one which consists of one person, to whom and his successors belongs the legal perpetuity which is denied to natural persons, is a corporation sole. To the former class belong banking, manufacturing and railway corporations, and incorporated mutual benefit and fraternal societies. To the latter the dignitaries of the Church of England, and all public officers who are invested with the attributes of a corporation by reason of their official position. The governor of a state,[2] and an officer to whom bonds are required to be made by statute, resemble corporations sole.[3] But sole corporations as they existed at common law are practically unknown in the United States. In the older states, where the religious establishment of the English church was introduced, the minister of the parish was seized of the freehold as in England. "We are not aware," said Chief Justice Shaw,[4] "that there is any instance of a sole corporation in this commonwealth, except that of a person who may be seized of parsonage lands, to hold to him and his successors in the same office, in right of his parish." "As for sole corporations," says Dr. Hammond,[5] "they have disappeared almost entirely from our law, not so much by any change in the law itself, as by the obsolescence of the ecclesiastical dignitaries, who furnished most of Blackstone's instances. Single persons holding some office or trust can take property or obligations upon themselves, and their respective successors, by properly worded instruments. Many public officers, treasurers, sheriffs, etc., are specially authorized by statutes to do the same. The law applicable to these cases is almost precisely that which a century ago would have been deemed peculiar to sole corporations, and yet the word is hardly ever applied to them."

[1] Fietsam v. Hay, 122 Ill. 293, 3 Am. St. R. 492, Wilgus' Cases.

[2] Governor v. Allen, 8 Humph. (Tenn.) 176, Wilgus' Cases.

[3] Polk v. Plummer, 2 Humph. (Tenn.) 500, 37 Am. Dec. 566.

[4] Overseers v. Sears, 22 Pick. (Mass.) 125, Wilgus' Cases.

[5] Hammond's Blackstone, I, 844. See also Kyd Corp., p. 20.

§ 17. **Ecclesiastical corporations.**—Corporations organized for the advancement of religion are common in England[1] and may exist in a few of the older states of the Union. But in the strict technical sense ecclesiastical corporations are at present unknown in this country.[2]

§ 18. **Incorporated religious societies.**—While the ecclesiastical corporations of the English law are unknown in this country, the incorporation of societies organized for the advancement of religion, and the more convenient transaction of business "relative to the temporalities thereof" is very common.[3] Such bodies are classed with those organized for literary, educational and charitable purposes and are provided for under the laws of most, if not all, the states. The property of the church is held by the corporation in trust and can not be diverted to other purposes.[4] Such organizations are favored by the law, and are frequently exempted from general taxation.[5] Civil courts will not control the internal management of incorporated religious societies, unless a civil or property right is invaded.[6] Thus a court will not interfere where the rights of a faction of the church to control its property depend mainly upon controverted matters of religious doctrine.[7] But where the doctrines of the church are thoroughly settled, those who adhere to such doctrines are entitled to control the property, although they constitute a minority of the membership.[8]

§ 19. **Charitable or eleemosynary corporations.**—Charitable corporations are formed for the administration of charitable

[1] 1 Bl. Com. 470; 2 Kyd Corp. 22-25.

[2] Robertson v. Bullions, 11 N. Y. 243, Wilgus' Cases.

[3] The church society may exist distinct from the corporation. Lilly v. Tobbein, 103 Mo. 477, 23 Am. St. R. 887; Hardin v. Trustees, 51 Mich. 137, 47 Am. R. 555, Wilgus' Cases.

[4] Brundage v. Deardorf, 55 Fed. 839; Dubs v. Egli, 167 Ill. 514, 47 N. E. Rep. 766; VanHouten v. McKelway, 17 N. J. E. 126.

[5] An exemption from general taxation does not exempt a religious corporation from liability for special assessments. See Elliott Pub. Corp., § 119.

[6] Waller v. Howell, 45 N. Y. Sup. 790, 20 Misc. (N. Y.) 236.

[7] Moseman v. Heitshousen, 50 Neb. 420, 69 N. W. 957. See note, 18 Am. St. R. 302.

[8] Smith v. Pedigo, 145 Ind. 361, 32 L. R. A. 838; Bear v. Heasley, 98 Mich. 279, 24 L. R. A. 615.

trusts and not for the profit of the members. They are in fact but the formal expression of an equitable trust. Such a corporation is a trustee selected by the donor of a charity for the purpose of managing the fund given for charitable uses. "Corporations of the eleemosynary sort," says Blackstone, "are such as are constituted for the distribution of the free alms or bounty of the founder, to such persons as he has directed, of which kind are all hospitals for the maintenance of the poor, sick and impotent, and all colleges."[1] Since the decision in the Dartmouth college case, it is the settled law of this country that the property of such a college is private property. Hence, the property of a private eleemosynary corporation, although charged with the maintenance of a college "or other public charity," is private property and not subject to the control of the legislature of the state.[2] In Illinois, under a statute it was held that the board of education was a private eleemosynary corporation and not a public corporation.[3] An insurance patrol company, organized to save and protect property from fire, which makes no distinction between insured and uninsured property, which has no stock and pays no dividends, but is supported by the voluntary contributions of insurance companies, is a public charitable corporation.[4]

§ 20. **Joint stock companies.**[5]—A joint stock company has some of the characteristics of a partnership and a corporation. It is in fact a partnership with the outward form of a corporation, and endowed by statute with some of the powers and privileges of a corporation. Except when expressly restricted by statute, the members of such an association are liable as partners.[6] The interests of the members are represented by shares. It is in fact "a partnership made up of many persons

[1] Blackstone (Hammond's ed.), I, 471; Kyd Corp. 25, 29; Kent's Com. (Barnes' ed.), II, 274; American Asylum v. Phœnix Bank, 4 Conn. 172, 10 Am. Dec. 112. See also Dartmouth College v. Woodward, 4 Wheat. 518, Wilgus' Cases.

[2] State v. Neff (Ohio), 28 L. R. A. 409.

[3] Board of Education v. Greenbaume, 30 Ill. 610; Board of Education v. Bakewell, 122 Ill. 339.

[4] Fire Ins. Patrol v. Boyd, 120 Pa. St. 624, 6 Am. St. R. 745.

[5] For distinction between corporations and partnerships, joint stock companies, unincorporated companies, cost book mining companies, see Wilgus' Cases Corps.

[6] Hedges App., 63 Pa. St. 273; People v. Coleman, 133 N. Y. 279, 31 N. E. Rep. 96; Frost v. Walker, 60 Me. 468; Batty v. Adams Co., 16 Neb. 44.

acting under articles of association for the purpose of carrying on a particular business, and having a capital stock divided into shares transferable at the pleasure of the holder.'"[1] The shares are transferable without the consent of the other members.[2] Such bodies are created by contract and do not require authority from the state, although in many states there are statutory provisions for their organization.[3] The creation of a corporation "merges in the artificial body and drowns in it the individual rights and liabilities of the members, while the organization of a joint stock company leaves the individual rights and liabilities unimpaired and in full force.'"[4] A joint stock company is generally sued as a partnership; and in the absence of statutory exemptions, each member is liable for all the debts of the company after the joint property is exhausted.[5]

[1] Att'y-Gen. v. Mercantile, etc., Ins. Co., 121 Mass. 524; Edwards v. Warren L. W. Co., 168 Mass. 564, 38 L. R. A. 791, Wilgus' Cases. For short sketch of history of joint stock companies see Van Sandan v. Moore, 1 Russ. Ch. 441. See also Gleason v. McKay, 134 Mass. 419, Wilgus' Cases; Lewis v. Tilton, 64 Iowa 220, 52 Am. R. 436, Wilgus' Cases (Unincorporated Association); Belton v. Hatch, 109 N. Y. 593, 4 Am. St. R. 495, Wilgus' Cases (Stock Exchange); Skillman v. Lockman, 23 Cal. 198, Wilgus' Cases (Cost Book Mining Company).

[2] Burnes v. Pennell, 2 H. of L. Cas. 520; Willis v. Chapman, 68 Vt. 459, 35 Atl. Rep. 459.

[3] People v. Coleman, 133 N. Y. 279.

[4] People v. Coleman, 133 N. Y. 279.

[5] Taft v. Ward, 106 Mass. 518; Frost v. Walker, 60 Me. 468; Butterfield v. Beardsley, 28 Mich. 412.

CHAPTER 2.

THE CREATION, ORGANIZATION, AND CITIZENSHIP OF CORPORATIONS.

I. The Creation and Organization.

§ 21. In general.
22. By what authority.
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I. The Creation and Organization.

§ 21. **In general.**—Individuals can not as a matter of right assume the powers and privileges of a corporation. These artificial bodies are created, not by the will of natural persons, but by the exercise of the sovereign power of the state, which thus confers upon certain designated persons the franchise of doing what they have no right to do without such special authority. This privilege of conferring special powers and rights upon favored individuals was formerly considered the "fairest flower of the prerogative."

§ 22. **By what authority.**—The consent of the sovereign is therefore necessary to a legal incorporation. In England it was the privilege of the king to create corporations; but they are now usually organized under the authority of acts of parliament. In the United States and the several states of the Union the legislative department only can create or authorize the creation of corporations; but this power is sometimes, under proper constitutional authority, delegated to the courts.

§ 23. **Essentials of legal incorporation.**—In order that there may be a legal incorporation, there must be a legislative grant of authority, an agreement between the incorporators, and an acceptance of the grant. The necessity for legislative authority has been already referred to.

§ 24. **Agreement between incorporators.**—It is necessary that there should be a contractual relation between the parties forming the corporation.[1] This agreement may be entered into in various ways, and may be implied from the acts of the parties. No particular form is necessary, unless prescribed by charter or statute. The acceptance of the charter or a subscription for shares is ordinarily sufficient evidence of an agreement to form a corporation according to the terms of the charter.[2]

[1] Green v. Knife Falls Boom Co., 35 Minn. 155, Wilgus' Cases.

[2] Morawetz Priv. Corp., I, §§ 24, 25; Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42. Mr. Clark, Private Corporations, §§ 27 and 86, taking issue on this point, says the contract is only between the subscriber and the corporation, and criticises Mr. Taylor's and Mr. Morawetz's views. Mr. Beach, Private Corporations, § 23, and the inference from Story's opinion in the Dartmouth College Case, would lead to the conclusion that there is a contract between the members and the corporation, and among the members themselves.

§ 25. **Acceptance of the grant.**—The charter of a corporation is merely an enabling act which must be accepted by the grantees before any rights can be claimed under it. If not accepted within a reasonable time, its legal effect expires.[1] Like all offers, it may be withdrawn at any time before acceptance.[2] The acceptance can be by those only to whom the offer was made,[3] and must be as a whole, and unconditional, unless it appears that it was the legislative intent that it may be accepted in part and rejected in part.[4] The acceptance must be by the corporators in their constituent capacity, and the act of acceptance must be done within the borders of the state.[5] No particular formalities are necessary in order to constitute an acceptance of a charter, and if no conditions are attached to a grant, user sufficient to show an intention to accept is sufficient.[6] The question of acceptance is one of fact for the jury.[7]

§ 26. **Delegation of power to charter corporations.**—Parliament being free from any constitutional limitations, and absolute in its legislative authority, may license another to grant corporate franchises. But in the United States, where the legislature itself exercises delegated power, the principle *delegata potestas non potest delegare* applies. Hence, a general power to confer corporate franchises can not be delegated by the legislature of the state to any other body.[8]

§ 27. **Delegation of ministerial duties.**—The principle of the preceding section does not prevent the delegation of ministerial duties. Thus the legislature may properly provide that

[1] State v. Dawson, 16 Ind. 40; State v. Bull, 16 Conn. 179; Smith v. Silver, etc., Co., 64 Md. 85, 54 Am. Rep. 760; Quinlin v. Houston, etc., R. Co., 89 Tex. 356.

[2] Lincoln Bank v. Richardson, 1 Greenl. 79, 10 Am. Dec. 34.

[3] Rex v. Amery, 1 T. R. 575.

[4] Rex v. Westwood, 2 Dow. & Clark 21; Lyons v. Orange, etc., R. Co., 32 Md. 18.

[5] Miller v. Ewer, 27 Me. 509.

[6] State v. Sibley, 25 Minn. 387; Miss. & R. R. B. Co. v. Prince, 34 Minn. 79; Louisville Tr. Co. v. L., etc., R. Co., 75 Fed. Rep. 433; Bank v. Lyman, 20 Vt. 666; Bangor, etc., R. Co. v. Smith, 47 Me. 34. Acceptance by a majority of members, see St. Paul Div. v. Brown, 11 Minn. 356, Gil. 254; Jackson v. Walsh, 75 Md. 304, 23 Atl. Rep. 778.

[7] Hammond v. Straus, 53 Md. 1.

[8] Cooley Const. Lim. 141; Thorne v. Cramer, 15 Barb. (N. Y.) 112. See Thomas v. Dakin, 22 Wend. (N. Y.) 110, Wilgus' Cases. But see 6 Am. & Eng. Enc. of Law, 2d ed., p. 1021, concerning delegation of legislative functions. Also delegation to territorial legislatures. Riddick v. Amelin, 1 Mo. 5, Wilgus' Cases, and delegation to Regents of University of New York.

some designated officer shall issue a certificate to the effect that the incorporators have complied with certain statutory requirements before the incorporation shall take effect.[1] With reference to such a statute the court said:[2] "The act rests upon the legislative will, and in no way depends for its vitality upon the action of the commissioners. * * * The commissioners perform no legislative act; they enact no laws; they simply perform administrative acts in carrying the law into effect and applying it."

Hence, in the absence of an authorizing provision in the constitution, the legislature can not delegate to a court the power to create corporations. But a distinction is made between *creating* and *organizing*, and even in the absence of such a provision the legislature may provide that the courts shall supervise the organizing of incorporations under the provisions of a general incorporation act. In such cases the court determines whether the incorporators have complied with the law, and when they have done so, issues its certificate or charter to that effect.[3]

§ 28. **Power of congress to create corporations.**—The congress of the United States may create a corporation when such a body is an appropriate means for carrying into execution any of the express or implied powers of the national government. But it is as a means and not as an end that congress may create corporations.[4] Thus the national legislature has in the exercise of this power created national banking corporations;[5]

[1] Franklin Bridge Co. v. Wood, 14 Ga. 80; People v. Nelson, 46 N. Y. 477.

[2] In re New York, etc., R. Co., 70 N. Y. 327.

[3] Franklin Bridge Co. v. Wood, 14 Ga. 80.

[4] McCulloch v. Maryland, 4 Wheat. 316; Story Const. Sec. 1266; Hare, Am. Const. Law, §§ 98, 105, 111, 249, 1310. See an article on "National Corporations" in 21 Cent. L. J. 428. Both Madison and Pinckney introduced resolutions in the constitutional convention, enumerating the power to create corporations among the powers of congress. They were referred to a committee and never reappeared. Madison's Journal of Debates (Scott's ed.), p. 549. See also p. 726, where the objections to such a grant are stated by King.

[5] McCulloch v. Maryland, 4 Wheat. 316; Osborne v. United States Bank, 9 Wheat. 738; Juilliard v. Greenman, 110 U. S. 421, 445. For the act creat-

savings banks; institutions of learning; religious, benevolent and educational societies; manufacturing, agricultural, mechanical, insurance, transportation, railroad, market, and cemetery corporations; and boards of trade within the District of Columbia,[1] and railway corporations operating lines extending into two or more states.[2] Congress has also created corporations for building a Nicaragua Canal,[3] and also passed a general law providing for the formation of national trades-union organizations, with branches in the states.[4]

ing the present national banking system, see 12 U. S. Statutes at Large, 665.

[1] Compiled Statutes of Dist. of Columbia, ch. 15; Hadley v. Freedman's Saving, etc., Co., 2 Tenn. Ch. 122; Williams v. Creswell, 51 Mass. 817; Daily v. National, etc., Co., 64 Ind. 1.

[2] California v. Central Pac. R. Co., 127 U. S. 1, 39; Union Pac. R. Co. v. Hall, 3 Dill. (C. C.) 515, s. c. 91 U. S. 343. In Luxton v. North River Bridge Co., 153 U. S. 525, the supreme court of the United States said: "The congress of the United States, being empowered by the constitution to regulate commerce among the several states, and to pass all laws necessary or proper for carrying into execution any of the powers specifically conferred, may make use of any appropriate means for this end. As said by Chief Justice Marshall, 'The power of creating a corporation, though appertaining to sovereignty, is not, like the power of making war, or levying taxes, or of regulating commerce, a great substantive and independent power, which can not be implied as incidental to other powers, or used as a means of executing them. It is never the end for which other powers are exercised but a means by which other objects are accomplished.' Congress, therefore, may create corporations as appropriate means of executing the powers of government, as, for instance, a bank for the purpose of carrying on the fiscal operations of the United States, or a railroad corporation for the purpose of promoting commerce among the states. McCulloch v. Maryland, 4 Wheat. 316, 411, 422; Osborn v. Bank of United States, 9 Wheat. 738, 861, 873; Union Pac. R. Co. v. Myers ('Pacific R. Removal Cases'), 115 U. S. 1, 18; California v. Pac. R. Co., 127 U. S. 1, 39. Congress has likewise the power, exercised early in this century by successive acts in the case of the Cumberland or National Road from the Potomac across the Alleghenies to the Ohio, to authorize the construction of a public highway connecting several states. See Indiana v. United States, 148 U. S. 148. And whenever it becomes necessary for the accomplishment of any object within the authority of congress, to exercise the right of eminent domain and take private lands, making just compensation to the owners, congress may do this with or without a concurrent act of the state in which the lands lie. Van Brocklin v. Tennessee, 117 U. S. 151, 154, and cases cited; Cherokee Nation v. Kansas R. Co., 135 U. S. 641, 656. From these premises the conclusion appears to be inevitable that, although congress may, if it see fit, and as it has often done, recognize and approve bridges erected by authority of two states across navigable waters between them, it may, at its discretion, use its sovereign powers, directly or through a corporation created for that object, to construct bridges for the accommodation of interstate commerce by land, as it undoubtedly may to improve the navigation of rivers for the convenience of interstate commerce by water. 1 Hare, Const. Law, 248, 249."

[3] 25 U. S. Stats. 673.

[4] 49 Cong., 1st Sess., ch. 567 (1886); 1 Supp. R. S. 498.

§ 29. **Ratification of claim of corporate franchise.**—Any act of the legislature which indicates an intention to recognize the existence of a corporation will amount to a ratification of a claim of corporate existence. The legislature may ratify when it may create or authorize. Thus a statute annexing other territory "to the town of A," by implication makes it a town, if it was not one before,[1] but "no greater effect can be attributed to a statute than appears to have been intended by the legislature enacting it."[2] Such a ratification not only legalizes the existence of a corporation, but cures the illegality of corporate acts done before the act of ratification was passed.[3]

§ 30. **Corporations by prescription.**—A corporation is said to exist by prescription if its commencement can not be shown, and the grant of a charter is presumed from long continued use of the corporate franchise. This is the doctrine in the United States as regards public corporations,[4] and the same principles have been held to apply to private corporations,[5] although the rule is that where there are general incorporation laws enacted under constitutions prohibiting the creation of any corporation, except municipal by a special act, there can be no private corporations by prescription (which is a tacit sovereign recognition), nor even by express legislative recognition. In other words, where the claim of corporate existence and right to exercise a corporate franchise is called in question by the proper proceedings, nothing less than proof of substantial compliance with statutory provisions will support the claim.[6]

§ 31. **Creation by implication.**—No particular form of words is essential to authorize the creation of a corporation, and the legislative intent may be inferred from general and inexact terms.[7]

[1] Bow v. Allentown, 34 N. H. 351. As to power of ratification in general, see Katzenberger v. Aberdeen, 121 U. S. 172.

[2] Thornton v. Marginal, etc., Co., 123 Mass. 32.

[3] Basshor v. Dressel, 34 Md. 503; Grand Trunk R. Co. v. Cook, 29 Ill. 237; St. Louis R. Co. v. N. W. R. Co., 2 Mo. App. 69; State v. Steele, 37 Minn. 428.

[4] Jameson v. People, 16 Ill. 257; People v. Maynard, 15 Mich. 463.

[5] Rose Hill, etc., Co. v. People, 115 Ill. 133; Green v. Dennis, 6 Conn. 298; Robie v. Sedgwick, 35 Barb. 319; White v. State, 69 Ind. 273.

[6] People v. Cheeseman, 7 Colo. 376; People v. Stanford, 77 Cal. 360.

[7] O'Leary v. Board of Com'rs, 79 Mich. 281, 19 Am. St. Rep. 169.

"Any expression showing an intent on the part of the legislature to confer the right to exercise corporate power is sufficient, and this intention may be deduced from the whole of the legislative act.'"[1] The question whether an aggregation of individuals is a corporation is to be determined rather by faculties and powers conferred upon it than by the name or description given to it.[2] Thus, when powers are granted which can not be exercised or enjoyed without corporate existence, the further right to be a corporation will be implied, although the statute granting the powers expressly declares that the grantee of the power or franchise shall not be deemed a corporation.[3] So, if powers and privileges are conferred upon the inhabitants of a certain district, or territorial area, and if they can not be enjoyed or exercised, and the purposes intended can not be attained without acting in a corporate capacity, an incorporation to this extent is created by implication, and the intent of the legislature can be shown constructively as well as expressly.

§ 32. **Methods of legislative action.**—Until within recent years all corporations were created by special legislation, but such legislation is now generally forbidden by constitutional provisions.[4] By a federal statute territorial legislatures are

[1]McAuley v. R. Co., 83 Ill. 348; Mead v. Ry. Co., 45 Conn. 199; Andes v. Ely, 158 U. S. 312; Dean v. Davis, 51 Cal. 406.

[2]Edgeworth v. Wood, 58 N. J. S. 463.

[3]Liverpool, etc., Ins. Co. v. Mass., 10 Wall. 566, s. c. 100 Mass. 531; Thomas v. Dakin, 22 Wend. 108; Dunn v. University of Oregon, 9 Ore. 357, Wilgus' Cases.

[4]Stimson Am. Stat. Law I, § 441; Binney's Restrictions on Special Legislation; Elliott Pub. Corp., ch. 4. Thus the Const. of Minn., art. 10, § 2, provided that "no corporations shall be formed under special acts except for municipal purposes." In 1892 an amendment to the consitution was adopted which provides that "in all cases when a general law can be made applicable, no special law shall be enacted; and whether a general law could have been made applicable in any case is hereby declared a judicial question, and as such shall be judicially determined without regard to any legislative assertion on that subject. The legislature shall pass no local or special law regulating the affairs of or incorporating, erecting or changing the lines of any county, city, village, township, ward or school district, * * * granting to any corporation, association or individual any special or exclusive privilege, * * * or franchise whatever. * * * The legislature may repeal any existing special or local law, but shall not

prohibited from granting private charters.[1] The language of these provisions varies and many of them apply to certain kinds or classes of corporations only, but the tendency of modern legislation is toward restricting the field of special legislation.

§ 33. **Constitutional limitations.**—It is extremely difficult to determine just what power the legislature can exercise over corporations by special act without violating a constitutional provision forbidding the creation of corporations by special acts.[2] It certainly is not deprived of the power to regulate by the prohibition of the power to create,[3] as it is one thing to create or bring into being a corporation, and quite another to deal with it as an existing entity.[4] The provision of the constitution of Minnesota which forbade the formation of corporations by special act was held not to prevent the legislature from extending the duration of a corporate franchise previously granted to a railroad company for a limited time;[5] nor from authorizing the change of a corporation originally organized as a mutual insurance company into a stock company.[6] In other states, however, it is held that when the legislature "can not pass any special act for the incorporation of cities and towns, it is prohibited from passing any act having for its object the amendment of such act,"[7] and the present constitution of Minnesota provides that while the legislature may repeal existing special or local laws, it shall not amend, extend or modify any of the same.[8] "A prohibition from creat-

amend, extend or modify any of the same." Laws of 1893, p. 3. This amendment is construed in Board, etc., v. Cooley (Minn.), 58 N. W. Rep. 150.

[1]U. S. Rev. Stat., § 1889. See Carver Mercantile Co. v. Hulme, 7 Mont. 566.

[2]See Elliott Pub. Corp., ch. 4, and authorities cited.

[3]Attorney-General v. North American Ins. Co., 82 N. Y. 172, 183.

[4]Southern Pac. R. Co. v. Orton, 32 Fed. Rep. 457, Wilgus' Cases.

[5]Cotton v. Miss., etc., Co., 22 Minn. 372.

[6]St. Paul, etc., Ins. Co. v. Allis, 24 Minn. 75.

[7]Town of McGregor v. Baylies, 19 Iowa 43; Ex parte Pritz, 9 Iowa 30; San Francisco v. Spring Valley, 48 Cal. 493.

[8]Amend. of 1892. In Minnesota, prior to the constitutional amendment of 1881, the existing constitutional provision had been practically nullified by judicial construction. Many of the great railroad corporations of

ing corporations by special act,'' says Morawetz,[1] ''undoubtedly does not, in terms, prohibit the legislature from passing a special law altering the charter of an existing corporation. But it is plain that a constitutional provision can not be avoided and practically annulled by a subterfuge. A special law altering the charter of an existing corporation and practically changing it must, therefore, be deemed in violation of a constitutional prohibition against the creation of corporations by special act.''

§ 34. **By consolidation.**—The legislature may provide for the creation of a corporation by the consolidation of existing

the state were organized prior to the adoption of the constitution under territorial charters. See Edgerton's Railroad Laws. In 1861 the present St. Paul & Duluth Railway was organized under one of these territorial charters by striking out the directors named in the act and inserting others, by changing the route of the road therein named and various other important amendments. The question of the validity of this legislation was submitted to the attorney-general, who rendered an opinion adverse to its validity. Opinions of attorney-general (2d ed.), 190. The question then came before the supreme court, which decided it in the same way, but the membership of the court having changed, upon reargument, the act was upheld, largely upon the ground that a practical construction had been placed upon the act, which had been acquiesced in by the legislature and the people, and that private and public interests of great magnitude, which had grown up on the faith of that construction, would be impaired by an adverse decision. Ames v. Lake Superior, etc., R. Co., 21 Minn. 241; Cotton v. Miss., etc., Co., 22 Minn. 372; Cent. R. Co. v. Clark, 23 Minn. 422; St. Paul, etc., Ins. Co. v. Allis, 24 Minn. 75. These were all cases of amendments of territorial charters, and the question whether a corporation could be organized under the general laws of the state and then receive by special grant distinct corporate franchises, remained open until 1886, when it came before the court in the case of Green v. Knife River Falls Boom Corp., 35 Minn. 155, A corporation had been organized under the general laws to build and maintain booms in the St. Louis river, after which a special act was passed, which conferred upon it the right to exercise the power of eminent domain by condemning lands which were flowed by its dams, or taken for its use, to take tolls, and to obstruct navigable parts of the river. The court followed Ames v. Lake Superior, etc., R. Co., 21 Minn. 241, and said: ''This constitutional provision was open to construction, and during a long course of legislation the practical construction placed upon it by the legislature and people has been a liberal one with respect to amendments, and the court would be very slow to change it at this late day.''

[1] Priv. Corp. I, § 10. An act changing the name of a corporation is not the grant of a private charter or a special privilege. Wells, Fargo & Co. v. Oregon R. Co., 8 Sawy. (C. C.) 601.

corporations.[1] The word consolidation is used somewhat loosely, but commonly describes the union of the stock, property or franchises of two or more corporations by which their affairs are permanently, or for a long period of time, placed under one management. The English decisions use the word amalgamation to express the idea of the fusion of two or more corporations into a new one, as well as the merger of one corporation into another. The American decisions use the word consolidation to express what the English call a true amalgamation.[2] Legislative consent is necessary to a legal consolidation;[3] and an attempt to consolidate without authority is a ground for forfeiting the corporate charter. Every consolidation does not result in the creation of a new corporation,[4] although the general rule is that consolidation works a dissolution of the previously existing corporations, and the creation of a new corporation with property, liabilities and stockholders derived from those which pass out of existence.[5]

[1] Adams v. Yazoo, etc., R. Co., 24 So. Rep. (Miss.), 317. "The fact that it is formed out of old, defunct corporations does not make it any the less a corporation created by the legislature. It is not the material out of which it is formed, but the plastic hand which formed it, that we are to look to for its character and status under the constitution." Shields v. State, 26 Ohio St. 86. As to consolidation of parallel and competing railway corporations, see Pearsall v. Great Northern R. Co., 161 U. S. 646.

[2] Dougan's case, 28 L. Times N. S. 60. As to meaning of amalgamation, Empire, etc., Co. v. Ex parte Bagshaw, L. R. 4 Eq. 341; Wall v. London, etc., Corp., 67 L. J. R. (Ch. D.) 596 (1898).

[3] Acts authorizing consolidation are acts of incorporation. Ohio, etc., R. Co. v. People, 123 Ill. 467. As to power of the legislature to authorize consolidation, see Botts v. Simpkinsville, etc., Co., 88 Ky. 54, 2 L. R. A. 594.

[4] It is a question to be determined by the nature of the union and the legislative intent. See Farnum v. Blackstone, etc., Corps., 1 Sum. C. C. 46; United States v. Southern, etc., R. Co., 45 Fed. Rep. 596; John Hancock, M. L. I. Co. v. Worcester, etc., R. Co., 149 Mass. 214; Day v. Worcester, etc., R. Co., 151 Mass. 302; Hirschl Consol. of Corp., p. 184, *et seq.* The mere purchase of one corporation by another does not consolidate the corporations. Gulf, etc., R. Co. v. Newell, 73 Tex. 334, 15 Am. St. R. 788.

[5] Pullman, etc., Co. v. Mo., etc., R. Co., 115 U. S. 587; Gray v. National Steamship Co., 115 U. S. 116; McMahon v. Morrison, 16 Ind. 172, 79 Am. Dec. 418; People v. New York, etc., R. Co., 15 N. Y. Supp. 635; People v. Cook, 110 N. Y. 443, 111 N. Y. 688; Fitzgerald v. Mo., etc., R. Co., 45 Fed. Rep. 812. See Ewing v. Composite, etc., Co., 169 Mass. 72. The new corporation may be foreign although the old one was domestic. Ohio, etc., R. Co. v. People, 123 Ill. 467. In Kansas, etc., R. Co. v. Smith, 40 Kan. 192.

The procedure for consolidation is prescribed by the statute, and, as in all proceedings to create a corporation, the provisions which the statute makes conditions precedent must be substantially complied with before a *de jure* corporation is created.[1] The consolidation sometimes takes the form of a lease[2] or the purchase by one corporation of the shares of another.[3] But whatever its form, it must be under legislative authority of such a character as to authorize the creation of a new corporation.[4]

II. Organization Under General Incorporation Laws.

§ 35. **In general.**—The franchise of being a corporation was originally granted by the legislature as a favor to the incorporators, but the policy of the state now is to encourage incorporation. In almost all the states there are general incorporation laws under which parties may freely become incorporated by complying with the requirements of the statute.[5]

§ 36. **General requirements.**[6]—These general statutes vary in detail, but usually provide that the persons purporting to form the corporation, not less than a designated number, shall sign and acknowledge an instrument called the articles of incorporation, which shall state the name of the corporation, the general nature of the business and the principal place of transacting the same, the time of commencement and the period of continuance of the corporation, the amount of capital stock and

it was held an appeal was abated by consolidation. Hirschl Consol. of Corps., p. 197, *et seq.*

[1]Commonwealth v. Atl., etc., R. Co., 53 Pa. St. 9; Tuttle v. Mich., etc., R. Co., 35 Mich. 247; Leavenworth Co. v. Chicago, etc., R. Co., 25 Fed. Rep. 219. An attempted consolidation may result in a *de facto* corporation only. Marshall Foundry Co. v. Killian, 99 N. C. 501, 6 Am. St. R. 539.

[2]State v. Atchison, etc., R. Co., 24 Neb. 143.

[3] Central R. Co. v. Georgia, 92 U. S. 665; Hill v. Nisbet, 100 Ind. 341.

[4] Clearwater v. Meridith, 1 Wall. (U. S.) 25; Shrewsbury, etc., R. Co. v. Stour Valley R. Co., 2 DeGex, M. & G. 866. The new corporation exists as of the date of the consolidation. Shields v. State, 26 Ohio St. 86.

[5] For the history of the practice of incorporation, see chapter on "Freedom of Incorporation," in Baldwin's Modern Political Institutions.

[6] See Wilgus' Cases, Schemes of Incorporation under Special Acts, and Schemes of Organization under General Laws.

how to be paid in, the highest amount of indebtedness or liability to which the corporation shall be subject, the names and places of residences of the incorporators, the number and amount of the shares of the capital stock, the names of the first board of directors, and in what officers or persons the management of the affairs of the corporation shall be vested. When such articles are published for a certain period, filed in the office of the secretary of state and in certain offices of record, a certificate of incorporation is issued by the secretary of state reciting that the provisions of the statute have been complied with and that the parties are properly incorporated. In many states different statutes are enacted for the organization and regulation of different kinds of incorporations, such as railway, insurance, banking and manufacturing companies, and corporations with or without the power of eminent domain.

§ 37. **Purposes for which corporations may be organized.**— The purposes for which corporations may be organized under the general incorporation laws of the states cover almost the whole range of business and social action from "works of public utility"[1] to "other lawful business."[2] The language used in these statutes is very general, and is given liberal construction. Thus the maintenance of a wharf boat and steam elevator is a "work of public utility."[3] A corporation organized for educational purposes which charges tuition fees is not "a corporation for pecuniary profit."[4] An express company is engaged in "an industrial pursuit."[5] A corporation for "the purchasing and holding of real estate, subdividing the same into village lots and town sites" may be organized under a statute which, after enumerating certain kinds of business, adds "for other lawful business."[6] But when the general words follow other more specific words, it has been held that corpora-

[1]Glenn v. Breard, 35 La. An. 875.

[2]Brown v. Corbin, 40 Minn. 508. A corporation may be authorized to act as an assignee for creditors. Roane, etc., Co. v. Wis. Tr. Co., 74 N. W. Rep. 818 (Wis.).

[3]Glenn v. Breard, 35 La. An. 875.

[4]Santa Clara Female Academy v. Sullivan, 116 Ill. 375, 56 Am. Rep. 776.

[5]Wells v. N. P. R. Co., 23 Fed. Rep. 469.

[6]Brown v. Corbin, 40 Minn. 508.

tions can be organized only for purposes kindred to those specifically enumerated.[1] Perhaps, however, the better rule does not so limit such words.[2] When a statute authorizes the creation of corporations for certain purposes, a corporation organized for such purpose is legal, although it purports to have been organized under another statute.[3]

But where the purpose for which the corporation is stated to be organized will necessarily result in creating a monopoly the provision is void.[4]

The purposes for which a corporation is organized must be determined by the statements in its articles of incorporation.[5]

§ 38. **Substantial compliance with statutory requirements.** —"A substantial compliance with all the terms of a general incorporation law is prerequisite to the right of forming a corporation under it."[6] Thus, when the articles of incorporation are required to be signed by a designated number of persons, that number must sign.[7] But only substantial compliance is necessary, and non-compliance with provisions merely directory in their nature, such as a requirement that a verified certificate containing certain matters shall be filed by the directors, does not affect the legality of a corporation.[8] There may be irregularities which would afford a basis for proceedings by the state to oust the corporation of its franchises which would not affect the legality of its existence with respect to persons with whom it deals.[9] Even the state may be barred from such proceedings by lapse of time.[10]

[1] State v. International Inv. Co., 88 Wis. 512.

[2] State v. Cookins, 123 Mo. 56; Brown v. Corbin, 40 Minn. 508; York, etc., Assn. v. Barnes, 39 Neb. 440.

[3] State v. Minn., etc., Co., 40 Minn. 213.

[4] People v. Chicago, etc., 130 Ill. 268, 17 Am. St. R. 319.

[5] Detroit Driving Club v. Fitzgerald, 109 Mich. 670, 67 N. W. Rep. 899.

[6] People v. Montecito, etc., Co., 97 Cal. 276; Stowe v. Flagg, 72 Ill. 397; Bigelow v. Gregory, 73 Ill. 197; Abbott v. Omaha S. Co., 4 Neb. 416; State v. Wood, 84 Mo. 378; Rogers v. Danby Universalist Society, 19 Vt. 187; People v. Stockton, etc., R. Co., 45 Cal. 306; Eakright v. Logansport, etc., R. Co., 13 Ind. 404; Thornton v. Balcom, 85 Iowa 198; Sweney v. Talcott, 85 Iowa 103.

[7] State v. Critchett, 37 Minn. 13; Carey v. Morrill, 61 Vt. 598; Heinig v. Adams & Westlake, etc., Co., 81 Ky. 300; Clegg v. Hamilton, etc., Co., 61 Iowa 121; State v. Central, etc., Assn., 29 Ohio St. 399; People v. Montecito, etc., Co., 97 Cal. 276.

[8] Shakopee, etc., Works v. Cole, 37 Minn. 91; People v. Cheeseman, 7 Colo. 376; Walton v. Riley, 85 Ky. 413; State v. Foulkes, 94 Ind. 493; State v. Beck, 81 Ind. 500; Ex parte Spring Valley, etc., Works, 17 Cal. 132.

[9] Humphrey v. Mooney, 5 Colo. 282.

[10] State v. Gordon, 87 Ind. 171.

§ 39. **Illustrations.**—The proper authentication and recording of the articles of association are necessary before there can be a legal incorporation ;[1] but a provision requiring a copy of the articles to be filed with a specified officer, such as register of deeds, is not necessary,[2] although the contrary is held in some cases.[3] The omission to state the residence of the incorporators,[4] signing the initials instead of the full Christian name,[5] the statement that "said corporate stock shall consist of five hundred shares at one hundred dollars per share" when the statute requires that the certificate of incorporation "shall state the amount of the capital stock,"[6] a statement that the corporation shall exist "at least forty years," when the statute required that the certificate state "the term of existence not to exceed forty years" are not such defects as will prevent legal incorporation.[7] The omission of the words "in good faith" from a certificate which is required to state "in substance that said amount of stock has been subscribed, and that ten per cent. in cash thereon has been actually and in good faith paid in," when it appears elsewhere in the body of the certificate that the ten per cent. has been actually in good faith paid in, is immaterial.[8]

§ 40. **Conditions precedent to organization of corporation de jure.**[9]—Those provisions of the general statutes, which are intended to be conditions precedent to incorporation, must be

[1]Stowe v. Flagg, 72 Ill. 397; People v. Montecito, etc., Co., 97 Cal. 276.

[2]Hurt v. Salisbury, 55 Mo. 310; Mokelumne Hill, etc., Co. v. Woodbury, 14 Cal. 425; Compare, Indianapolis, etc., Co. v. Herkimer, 46 Ind. 142; People v. Chambers, 42 Cal. 201; Hammond v. Strauss, 53 Md. 1. A failure to comply with a provision requiring the payment of a fee to the state before incorporation does not prevent legal incorporation. Hughesdale Mfg. Co. v. Vanner, 12 R. I. 491. *Contra*, Maryland, etc., Works v. West End Imp. Co., 87 Md. 207, 39 L. R. A. 810.

[3]Childs v. Hurd, 32 W. Va. 99; Doyle v. Mizner, 42 Mich. 332; Garnett v. Richardson, 35 Ark. 144; Indianapolis, etc., Co. v. Herkimer, 46 Ind. 142; First Nat. Bank v. Davies, 43 Iowa 424; Abbott v. Omaha, etc., Co., 4 Neb. 416; Capps & Hastings Prosp. Co., 40 Neb. 470, 58 N. W. Rep. 956; Martin v. Deetz, 102 Cal. 55, 36 Pac. Rep. 369.

[4]State v. Foulkes, 94 Ind. 493; Rogers v. Danby Univ. Soc., 19 Vt. 187.

[5]State v. Beck, 81 Ind. 500.

[6]Hughes v. Antietam Mfg. Co., 34 Md. 316.

[7]Hughes v. Antietam Mfg. Co., 34 Md. 316.

[8]People v. Stockton, etc., R. Co., 45 Cal. 306.

[9]See, generally, Wilgus' Cases, Conditions Precedent to Corporate Existence *de jure*, *de facto*, and by estoppel.

strictly complied with before a *de jure* corporation is created. There is, however, a distinction, which must be observed, between conditions precedent to a legal incorporation and conditions precedent to the right to commence business. Until the former are substantially complied with there is no legal corporation. A failure to comply with the latter does not, however, affect the existence of the corporation.[1] Hence "the legal existence of a corporation is not terminated by the fact that it has violated its charter, as by carrying on business before conditions precedent imposed by the charter had been complied with."

No general rule can be stated other than that if it appears from the language of the statute that it was the intention of the legislature that the requirement should be complied with before the incorporation is completed, it is necessary that there should be substantial compliance.[2]

§ 41. **Articles of incorporation—Contents.**—General incorporation laws always provide for the execution by the incorporators of a certificate or articles of incorporation which must contain certain designated matters. Such articles have the effect of a charter,[3] hence there can be no incorporation when there are no articles,[4] and this is equally true where the articles are fatally defective by reason of not conforming to the essential requirements of the statute.[5] They may be defective by reason of omitting to state the number of directors,[6] the place of residence of the corporators,[7] the principal place of

[1]Holmes v. Gilliland, 41 Barb. (N. Y.) 568; Herrod v. Hamer, 32 Wis. 164; Charles River Bridge v. Warren Bridge, 7 Pick. (Mass.) 344.

[2]Childs v. Hurd, 32 W.Va. 67; Stowe v. Flagg, 72 Ill. 397; People v. Montecito, etc., Co., 97 Cal. 276.

[3]North Point, etc., Co. v. Utah, etc., Co. (Utah), 52 Pac. Rep. 168, 40 L. R. A. 851.

An attempted amendment of articles by *de facto* trustees is ineffectual. State v. Oftedal (Minn.), 75 N. W. Rep. 692.

[4]Abbott v. Omaha, etc., Co., 4 Neb. 416.

[5]N. Y. Cable Co. v. Mayor, 104 N. Y. 1; McCallion v. Hibernia, etc., Co., 70 Cal. 163.

[6]Reed v. Richmond, etc., R. Co., 50 Ind. 342.

[7]See Busenback v. Attica, etc., Co., 43 Ind. 265. A statement in the articles that the "office" of the corporation shall be in a certain city, does not sufficiently state the place in which the business shall be carried on. Ken-

business of the corporation,[1] or the amount of capital stock.[2] The object of the corporation must be stated in substantial compliance with the statute,[3] as the articles can not be aided, varied, or contradicted by parol evidence.[4]

If the time of existence is stated at a term in excess of that fixed by law, the corporation will continue for the statutory period.[5] A provision authorizing the board of directors to increase the capital stock without the consent of a majority of the stockholders, as required by statute, does not render the articles void.[6] The articles should contain only those provisions which are required by the statute, but the insertion of additional matter will not affect their validity, as it will be rejected as surplusage.[7] A provision that the articles shall

nett v. Woodworth Mason Co. (N. H.), 39 Atl. Rep. 585.

[1] Harris v. McGregor, 29 Cal. 124; People v. Beach, 19 Hun (N. Y.) 259; Clegg v. Hamilton, etc., Co., 61 Ia. 121.

[2] State v. Shelbyville, etc., Co., 41 Ind. 151; Thornton v. Balcom, 85 Iowa 198.

[3] People v. Cheeseman, 7 Colo. 376. For a stricter rule, see West v. Bullskin, etc., Co., 32 Ind. 138.

[4] Atty.-Gen. v. Lorman, 59 Mich. 157; People v. Beach, 19 Hun (N. Y.) 259; People v. Selfridge, 52 Cal. 331.

[5] People v. Cheeseman, 7 Colo. 376.

[6] Eastern, etc., Co. v. Vaughan, 14 N. Y. 546.

[7] Oregon R. Co. v. Oregonian R. Co., 130 U. S. 1; Albright v. La Fayette, etc., Co., 102 Pa. St. 411; Bigelow v. Gregory, 73 Ill. 197.

In New York and New Jersey, and under the National Banking Act, special provisions may be inserted in the articles.

It must be remembered that a *de facto* corporation may result, although the provisions of the statute are not complied with. In Johnson v. Schulin (Minn., 1897), 73 N. W. Rep. 147, the court said: "The plaintiff claims that because the articles of association were not signed by several persons, and were not recorded, there could be no corporation *de facto*, and rely in support of the claim upon the case of Johnson v. Corser, 34 Minn. 355, 25 N. W. Rep. 799. The claim ignores the fundamental principles applicable to corporations *de facto*; for if there had been a compliance with the statute in the respects complained of, a corporation *de jure* would have been created. Johnson v. Corser is not in point. That was a case where parties desiring to make a certain street improvement associated themselves together for that purpose, and signed articles of incorporation; but no attempt was made to give any publicity to them, by filing or recording or otherwise, until after the work had been performed for which the action was brought against the associates as partners. The plaintiffs also rely upon the case of Bergeron v. Hobbs, 96 Wis. 641, 65 Am. St. R. 85, 71 N. W. Rep. 1056. The case is directly in point, but its value as an authority is seriously impaired

state the purposes for which the corporation is formed and that it shall be unlawful for it to divert its funds to any other purposes is for the protection of the public, and does not under all circumstances affect the contracts of the corporation.[1]

§ 42. **Filing and publication of articles.**—The language of the statute must be carefully examined to determine whether the requirement of filing and recording of the articles is mandatory or directory. Ordinarily the filing of the articles with some state official, and their publication in some form, is a condition precedent to legal incorporation.[2] It has been held that the recording with the county recorder is a condition precedent.[3] The date of filing is not a part of the articles, and the fact of delivery and date of filing may be shown by parol evidence.[4] The incorporation is not invalidated by an erroneous recording in an improper book.[5] The surreptitious and fraudulent recording of articles of incorporation contrary to an agreement among the incorporators has no legal effect.[6]

§ 43. **Subscriptions for capital stock as a condition precedent.**—Unless made so by the governing statute, the subscription of the whole amount of the capital stock is not a condition precedent to the legal existence of a corporation.[7] The matter is, however, largely governed by statute. It has been held that merely making and filing articles of incorporation do not create a corporation where the stock has not been sub-

by an able and exhaustive dissenting opinion. Besides, it seems to be opposed to the weight of authority."

[1] Butterworth v. Kritzer Mills Co. (Mich.), 72 N. W. Rep. 990.

[2] Indianapolis, etc., Co. v. Herkimer, 46 Ind. 142; Clegg v. Hamilton, etc., Co., 61 Iowa 121; Childs v. Hurd, 32 W. Va. 66; Gent v. Mfg. Ins. Co., 107 Ill. 652, Wilgus' Cases.

[3] Cresswell v. Oberly, 17 Bradw. (Ill.) 281.

[4] Johnson v. Crawfordsville, etc., R. Co., 11 Ind. 280.

[5] Walton v. Riley, 85 Ky. 413.

[6] Ricker v. Larkin, 27 Ill. App. 625.

[7] Johnson v. Kessler, 76 Iowa 411; Schenectady, etc., R. Co. v. Thatcher, 11 N. Y. 102. The rule of the common law required that the capital stock should all be subscribed before the organization was completed. Schloss v. Montgomery T. Co., 87 Ala. 411, 13 Am. St. R. 51. See § 354 *infra*.

scribed or paid in or the directors chosen.[1] "Since a substantial compliance with the conditions of the statute is all that the law requires, except in the case of conditions precedent, it is generally held that where the governing statute requires a certain percentage of the stock to be paid in, it will be sufficient that the aggregate sum produced by such a percentage is paid in, and it will be immaterial by whom it is paid."[2]

§ 44. **Date of incorporation.**—A corporation exists from the time when the instrument of incorporation prescribed by statute is executed, acknowledged and recorded or filed for record, as required by the statute, and all conditions precedent performed. When the articles are required to be approved by some official, the incorporation dates from the time of such approval.[3]

§ 45. **Who may be incorporators.**—A corporation is commonly composed of natural persons, but its shares may be held by a state, a public or private corporation, a partnership, or by persons in a political capacity.[4] Any person capable of contracting may become an original shareholder of a private corporation,[5] and as the interest is assignable, it may be transferred to or held by women and children or by persons *non compos mentis*. But the right of membership in a particular corporation may be limited to a certain class, as the members of a certain profession or trade. Corporations are not "persons" within the meaning of general incorporation laws.[6] The

[1] State v. Fidelity, etc., Co., 49 Ohio St. 440, 16 L. R. A. 611.

[2] Thompson Corp., § 247. Notes given in fraud of a statute which requires the stock to be paid for in cash can not be defended against on the ground that the corporation had no authority to accept them. McLaren v. Pennington, 1 Paige (N. Y.) 102.

[3] Society v. Commonwealth, 52 Pa. St. 125. In Sparks v. Woodstock, etc., Co., 87 Ala. 294, it was held that the failure of a judge to make the necessary certificate did not prevent the corporation from coming into existence, when the proper antecedent steps had been taken. In State v. Fidelity, etc., Co., 49 Ohio St. 440, 16 L. R. A. 611, it was said that "articles of incorporation do not make a corporation; they are simply authority to do so."

[4] 10 Co. 29 b. See § 346, *infra*.

[5] The word "person" is construed to mean a person of full age. In re Globe, etc., Association, 63 Hun (N. Y.) 263. *Contra* in England. Re Nassau, etc., Co., 2 Ch. D. 610.

[6] See § 68, *infra*. But in England "person" includes "company" in the Companies Act of 1862. So one limited company may take shares in another. In re Barneds Banking Co., L. R. 3 Ch. 105; Royal Bank of India, L. R. 4 Ch. 252.

right of organizing a corporation is conferred upon individuals and not corporations. Unless the statute provides that the incorporators shall be residents of the state, no such conditions will be annexed, and the citizens of one state may organize a corporation under the laws of another state if they consider it to their advantage to do so.[1]

§ 46. **Number of incorporators.**—The statutes generally prescribe the minimum number of persons who may become incorporators, and this varies according to the nature and object of the corporation. When not expressly determined it seems that the law contemplates more than one incorporator. Thus under an act providing that "any number of persons may associate themselves together and become incorporated," one person can not form a corporation and thus conduct his business without personal liability.[2]

§ 47. **The corporate name.**—"When a corporation is erected a name must be given to it, and by that name alone it must sue and be sued, and do all legal acts, though a very minute variation therein is not material. Such name is the very being of its constitution, and though it is the will of the king that erects the corporation yet the name is the knot of its combination, without which it could not perform its corporate functions. The name of incorporation, says Sir Edward Coke, is a proper name or name of baptism, and therefore when a private founder gives his college or hospital a name, he does it only as a godfather, and by that same name the king baptizes the incorporation."[3]

The king or parliament in granting a patent usually designates or indicates by recitals the name by which the corpora-

[1]Under a law which authorizes "any number of persons not less than seven" to organize a corporation, citizens or residents of another state may organize under the law. Cent. R. Co. v. Pa. R. Co., 31 N. J. Eq. 475; Humphreys v. Mooney, 5 Colo. 282; Demarest v. Flack, 128 N. Y. 205; Lancaster v. Amsterdam Imp. Co., 140 N. Y. 576, 35 N. E. Rep. 964.

[2]Louisville, etc., Co. v. Eisenman, 94 Ky. 83, 19 L. R. A. 684, Wilgus' Cases.

[3]Bl. Com., I, 575. Bacon also calls the name the "knot of their combination." Abr. II (Am. ed.), 440.

tion shall be known.[1] But if a name is not given by the charter one may be assumed or acquired by usage and a contract made with a corporation under an assumed name may be enforced by either party.[2]

When a corporation has received a name it can only change the name in the manner prescribed by law.[3] A change of name does not affect the liabilities, duties, or property rights of a corporation.[4]

§ 48. **Protection of corporate name.** It has been held that the name of a corporation is a franchise, and that when the state has granted the franchise the corporation can not be restrained from using it, because it nearly resembles the name of an existing corporation, or will be liable to cause confusion.[5] The court in such a case accepts the certificate of the secretary of state as conclusive evidence of the right of the corporation to the name certified.[6] But the rule most consistent with principle is that a corporation will be protected in the use of its name upon the same equitable principles which protect persons in the use of trade names and trade-marks.[7] Judge

[1]Bacon, Abr. II, 441; "Names of Corporations," article in 23 Cent. L. J. 531.

[2]Clement v. City of Lathrop, 18 Fed. Rep. 885.

[3]Morris v. St. Paul, etc., R. Co., 19 Minn. 528, Gil. 459; Goodyear Rubber Co. v. Goodyear, etc., Co., 21 Fed. Rep. 276; Sykes v. People, 132 Ill. 32, 23 N. E. Rep. 391. An attempt to change a name by other means does not avoid a charter. O'Donnell v. Johns, 76 Tex. 363; Smith v. Plank Rd. Co., 30 Ala. 650; Wells, Fargo & Co. v. O. R. & N. Co., 8 Sawy. 600, 608. But in Cincinnati, etc., Co. v. Bate, 96 Ky. 356, 49 Am. St. R. 300, Wilgus' Cases, it was held that an unauthorized change of name by the members made them liable thereafter as partners.

[4]Welfly v. Shenandoah, etc., Co., 83 Va. 768; Hazlet v. Butler Univ., 84 Ind. 230; Bucksport, etc., Co. v. Buck, 68 Me. 81. "Though the name and style of the corporation and mode of electing members were changed, the identity of the body itself was not affected." Doe v. Norton, 11 M. & W. 913. All new suits on old obligations must be brought in the new name. Cotton v. Miss., etc., Co., 22 Minn. 372. A suit is not abated by change of name of corporation. Thomas v. Frederick School, 7 Gil. & J. 369.

[5]Boston, etc., Co. v. Boston, etc., Co., 149 Mass. 436. But see Armington v. Palmer (R. I.), 43 L. R. A. 95.

[6]Rice v. National Bank, 126 Mass. 300. The certificate of the auditor as to the right of a corporation to a certain name is not binding upon another body claiming the name. Grand Lodge v. Graham, 96 Iowa 592, 31 L. R. A. 133.

[7]Holmes v. Holmes, etc., Co., 37 Conn. 278, 9 Am. Rep. 324; Celluloid, etc., Co. v. Cellonite, etc., Co., 32 Fed. Rep. 94; Neb., etc., Co. v. Nine.

Thompson says: [1] "The better view is that the right of an existing corporation to the use of its corporate name, which is in the nature of a trade name, can not be infringed by a subsequent act of incorporation by the legislature, either by the direct grant of a charter to a corporation to be organized under a similar name, or through a ministerial officer of the state in granting a certificate of incorporation to a body of adventurers having a similar name."

Where the statute provides that the secretary of state shall not issue a certificate of incorporation under a name similar to that already assumed by another corporation, the secretary has a discretion which will not be controlled by mandamus.[2] As a general rule the name selected by a new corporation must not be identical with or too closely resemble that of an existing corporation.[3] The right to a name attaches upon the issuance of the license to incorporate, and before the incorporation is completed.[4] The absence of fraudulent intent is no defense in a suit for wrongfully assuming and using the name of another.[5] An injunction against the wrongful assumption and use of a corporate name may be granted in a suit by the owner of the name without the intervention of the state.[6]

27 Neb. 507, 43 N. W. Rep. 348. Foreign and domestic corporations with same name, Hazleton, etc., Co. v. Hazleton, etc., Co., 142 Ill. 494, 28 N. E. Rep. 245.

[1]Thompson Corps., Vol. I, § 296.

[2]State v. McGrath, 92 Mo. 355.

[3]International, etc., Co. v. International, etc., Co., 153 Mass. 271, 10 L. R. A. 758. In re U. S. Merc. Rep. Co., 115 N. Y. 176. A corporation known as the "Hygeia Water Ice Co." is not entitled to have the "New York Hygeia Ice Company, Limited," restrained from using the word "Hygeia," it not appearing that any one has been deceived. Hygeia Water Ice Co., 140 N. Y. 94.

[4]Illinois, etc., Co. v. Pearson, 140 Ill. 423. The right to a corporate name as a trade-mark is not a franchise. Hazleton, etc., Co. v. Hazleton, etc., Co., 142 Ill. 494, 28 N. E. Rep. 248.

[5]Armington v. Palmer (R. I.), 43 L. R. A. 95. As to rights of corporations in respect to names, see, generally, American Order v. Merrill, 151 Mass. 558, 8 L. R. A. 320; Int., etc., Co. v. Int., etc., Co., 153 Mass. 271, 10 L. R. A. 758; Chas. Higgins Co. v. Higgins, etc., Co., 144 N. Y. 462, 27 L. R. A. 42; Grand Lodge, etc., v. Graham, 96 Ia. 592, 31 L. R. A. 133; Supreme Lodge, etc., v. Improved, etc., 113 Mich. 133, 38 L. R. A. 658.

[6]Armington v. Palmer (R. I.), 43 L. R. A. 95, Wilgus' Cases.

§ 49. **Proof of incorporation—In direct proceedings.**—The evidence required to prove incorporation will depend upon the proceedings in which the issue is raised. In proceedings by the state for the purpose of testing corporate existence, the evidence must be sufficient to show substantial compliance with the terms of the law under which the corporation claims existence.[1] If the corporation is organized under a public act of the legislature, the court will take judicial notice of the law; but if the corporation was organized under a foreign law the statute must be pleaded and proved like any other fact.[2] Acceptance of the charter may be shown by any competent evidence that tends to show user.[3]

§ 50. **In collateral proceedings.**—When the issue of corporate existence is raised collaterally, it is sufficient to prove the existence of a *de facto* corporation. It must be shown that there is a valid law under which the company could have become a *de jure* corporation, a good faith attempt to incorporate under the law, and a user of the franchise.[4] The existence of a *de facto* corporation may be shown by parol evidence,[5] or a

[1]See § 40, *supra*.

[2]Jones Evidence, I, §§ 112, 120.

[3]Bank of Manchester v. Allen, 11 Vt. 302. If the fact of acceptance is recorded on the books of the corporation, the books are the best evidence. Hudson v. Carman, 41 Me. 84.

[4]State v. Murphy, 17 R. I. 698, 24 Atl. Rep. 473; Porter v. State, 141 Ind. 488, 40 N. E. Rep. 1601; Owen v. Shepherd, 59 Fed. Rep. 746, 8 C. C. A. 244. Caldwell, J., says: "The rule that the regularity of the organization of a corporation can not be inquired into collaterally has no application where individuals sued for services deny personal liability, and set up the existence of a corporation, to which the services were rendered." See § 72, *infra*.

[5]Calkins v. State, 18 Ohio St. 366, 98 Am. Dec. 121, Ann.; State v. Habib, 18 R. I. 558, 30 Atl. Rep. 462; Yakima Nat. Bank v. Knipe, 6 Wash. 348, 33 Pac. Rep. 834. When raised in pleading, proof of user good "prima facie," Rose Hill & E. R. Co. v. People, 115 Ill. 133, 3 N. E. Rep. 725. In Johnson v. Schulin (Minn.), 73 N. W. Rep. 147, it was held that for the purpose of showing a corporation *de facto* oral testimony not purporting to give the contents of corporate records or documents, tending to show that after an attempt to organize a corporation by the execution of articles of incorporation, the supposed corporation held meetings, adopted by-laws, elected officers, and did business as a corporation, is admissible without producing the corporate records or showing their loss. "On principle," said Chief Justice Start, "it would seem that where, as in this case, the defendants are seeking to avoid their liability as alleged

prima facie case may be made by the introduction of the books and records of the corporation.[1] It has been said that general reputation is sufficient to make a prima facie case.[2] Many states provide statutory methods for proving incorporation. In Michigan the statute provides that "In any suit wherein it shall become necessary or material to prove the incorporation of any corporation, evidence that such a corporation was doing business under a certain name shall be prima facie evidence of its due incorporation, or existence pursuant to law, and of its name."[3] When the statute provides that a certified copy of the articles of incorporation or of the certificate of incorporation shall be prima facie evidence of incorporation,[4] it does not exclude other competent evidence.[5]

For the purposes of the case it is generally sufficient to prove the facts sufficient to create an estoppel against the party raising the question.[6] It often becomes necessary to prove the existence of a corporation in criminal proceedings. As the question then arises collaterally, it is only necessary to show facts sufficient to establish a *de facto* corporation.

"On the trial parol proof was offered, admitted and given to the effect that an association of persons existed claiming to be a corporation under the name of the Michigan Southern and Northern Indiana Railroad Co., suing and being sued, having a common seal, and operating a railroad as such, and exercising the franchise of a corporation. * * * We are of the opinion, however, that the proof was both competent and sufficient."[7]

partners by showing that they were a *de facto* corporation with whom the plaintiffs dealt, the best evidence to prove the fact would be the sworn testimony of competent witnesses to what, in fact, was done." Thompson Corp., § 7735.

[1]Glenn v. Orr, 96 N. C. 413, 2 S. E. Rep. 538; Peake v. R. Co., 18 Ill. 88.

[2]Fleener v. State, 58 Ark. 98, 23 S. W. Rep. 1.

[3]Canal St. Gravel Road v. Paas, 95 Mich. 372.

[4]See Marshall v. Bank, 108 N. C. 639, 13 S. E. Rep. 182.

[5]Edelhoff v. State, 5 Wy. 19, 36 Pac. Rep. 627.

[6]U. S. Vinegar Co. v. Schlegel, 143 N. Y. 537, 38 N. E. Rep. 729. A contract made with the corporation in the corporate name is prima facie evidence of corporate existence as against the parties to the contract. Continental Ins. Co. v. Richardson, 72 N. W. Rep. 458 (Minn.).

[7]Embezzlement, Calkins v. State, 18

Where it is once shown that there is a charter, the exercise of corporate acts for many years will raise a presumption of incorporation.[1]

III. Promoters of Corporations.

§ 51. **Who are promoters.**—The term promoter is so well understood that a judge in charging a jury is not bound to define it.[2] "It is not a word of art; it must be understood by lawyers as it would by laymen."[3] A person who engages with an owner of land in the organization of a corporation which is intended to purchase the land, and who frames the prospectus, aids in procuring subscribers for stock, and becomes one of the first stockholders, is a promoter of the corporation.[4] But the mere fact that at the time when property was purchased the purchaser contemplated that a corporation would be organized for the purpose of acquiring the land does not make the purchaser a promoter of the corporation.[5]

§ 52. **Fiduciary position of promoters.**—The promoters can not be the agents of a principal not in existence, and can not bind the future corporation by their contract, but by various processes of reasoning, more or less unsatisfactory, they are held to occupy a fiduciary relation to the corporation which is to be created. From this relation it follows that they can not

Ohio St. 370; State v. Habib, 18 R. I. 558, 30 Atl. Rep. 462. Burglary, State v. Thompson, 23 Kan. 338, 33 Am. Rep. 165. Larceny, People v. Barrie, 49 Cal. 342; People v. Frank, 28 Cal. 507.

[1] See note to In re Gibbs, 157 Pa. St. 59, 22 L. R. A. 276. Long acquiescence raises a presumption of legal incorporation. Rose Hill & E. R. Co. v. People, 115 Ill. 133, 3 N. E. Rep. 725. *See* § 30, *supra*.

[2] Emma, etc., Co. v. Lewis, 4 C. P. Div. 396, 11 Ch. Div. 918.

[3] Bramwell, J., Twycross v. Grant, 2 C. P. Div. 503.

[4] Woodbury, etc., Co. v. Londenschlager, 55 N. J. Eq. 78, 35 Atl. Rep. 436.

In Yale, etc., Co. v. Wilcox, 64 Conn. 101, 25 L. R. A. 90, the court said: "A promoter has been defined to be a person who organizes a corporation. It is said to be not a legal but a business term, 'usefully summing up, in a single word, a number of business operations familiar to the commercial world, by which a company is generally brought into existence.'"

[5] Ladywell, etc., Co. v. Brookes, 35 Ch. Div. 400, 17 Am. and Eng. C. C. 22.

derive any personal advantage to the detriment of the corporation or its members, without a full and fair disclosure of their transactions to those who are entitled to act for the corporation. Hence, a promoter, when acting for the corporation, can not purchase property and sell it to the corporation at an advance, nor can he secretly receive a bonus from the vendor for negotiating the sale of his property to the corporation.[1]

§ 53. **Secret profits.**—Any secret profits made by the promoters of a corporation while acting for the corporation must be accounted for and may be recovered in equity by the corporation or its representatives.[2] In some cases it is held that a shareholder may maintain an action to recover his share of the profits,[3] or may sue in damages for the fraud.[4] Thus, where the promoter deceives the members of a corporation, as to the actual price paid for the property, or by collusion with the vendors is allowed a commission for making the sale, he is liable to the corporation for the profits accruing to him from the transaction.[5] A corporation may by means of a suit in equity, by or for its benefit, or by other appropriate means, rescind a sale of property to it and recover the consideration paid therefor, where the promoters were the real vendors and realized a profit on the property, concealing from the corpora-

[1]Chandler v. Bacon, 30 Fed. Rep. 538; Pittsburg Min. Co. v. Spooner, 74 Wis. 307, 42 N. W. Rep. 259; Woodbury, etc., Co. v. Loudenschlager, 55 N. J. Eq. 78, 35 Atl. Rep. 436; Plaquemines, etc., Co.v. Buck, 52 N. J. Eq. 219, 27 Atl. Rep. 1094; Emery v. Parrott, 107 Mass. 95; Yale, etc., Co. v. Wilcox, 64 Conn. 101, 25 L. R. A. 90; Simons v. Min. Co., 61 Pa. St. 202; Getty v. Devlin, 54 N. Y. 403; Burbank v. Dennis, 101 Cal. 90; Central Land Co. v. Obenchain, 92 Va. 130, 22 S. E. Rep. 876; Emma, etc., Co. v. Grant, 11 Ch. Div. 918; Erlanger v. Phosphate Co., L. R., 3 App. Cas. 1218. One who was originally a promoter can not, after the corporation has been in existence and engaged in business for more than a year, be held to a promoter's fiduciary duty to the corporation. Russell v. Rock River, etc., Co., 184 Pa. St. 102, 39 Atl. Rep. 21. Article in 16 Am. Law Rev. 671.

[2]Chandler v. Bacon, 30 Fed. 538; Cook v. Southern, etc., Co. (Miss.), 21 So. Rep. 795, Re Olympia, 67 L. J. Ch. N. S. 433.

[3]Emery v. Parrott, 107 Mass. 95.

[4]Getty v. Devlin, 54 N. Y. 403.

[5]Emma, etc., Co. v. Grant, 11 Ch. Div. 918; Simons v. Vulcan Oil Co., 61 Pa. St. 202.

tion and those associated with them in organizing it that they were personally interested in the sale.[1] One who organizes a corporation to purchase a patent while he already has a secret agreement with the owner by which he is to receive a part of the proceeds of the sale, and who obtains subscriptions to the stock of the company by stating that he is putting his money into the enterprise on the same basis as the others, must account to the other stockholders for the profits received under the secret agreement. The illegality of the contract because against public policy will not defeat the right of the corporation to recover the secret profits.[2]

§ 54. **Owners of property as promoters.**—The rule stated in the preceding section does not apply when the owner of property becomes the promoter of a corporation which it is intended shall become the purchaser of the property. In this case in acquiring the property the promoter acted for himself, and did not assume to act for the corporation. In the absence of false representations, and when the subscribers have an opportunity to ascertain the condition of the land, it is immaterial what the property may have originally cost the vendor.[3] The rule is well stated by Mr. Justice Sharswood:[4] "There are two principles applicable to all partnerships or associations for a common purpose of trade or business, which appear to be well settled on reason and authority. The first is that any man or number of men who are the owners of any kind of property, real or personal, may form a partnership or association with others, and sell that property to the association at any price which may be agreed upon between them, no matter what it may have originally cost, provided there be no fraudulent misrepresentations made by the vendors to their associates. They are not bound to disclose the profits which they may realize from the transaction. They were in no sense agents or

[1]Hebgen v. Koeffler (Wis.), 72 N. W. Rep. 745.

[2]Yale, etc., Works v. Wilcox, 64 Conn. 101, 25 L. R. A. 90.

[3]Milwaukee, etc., Co. v. Dexter, 99 Wis. 214, 74 N. W. Rep. 976, 40 L. R. A. 837; Plaquemines, etc., Co. v. Buck, 52 N. J. Eq. 219, 27 Atl. Rep. 1094; Franey v. Warner, 96 Wis. 222.

[4]Densmore, etc., Co. v. Densmore, 64 Pa. St. 43.

trustees in the original purchase, and it follows that there is no confidential relation between the parties, which affects them with any trust. It is like any other case of vendor and vendee. They deal at arm's length. Their partners are in no better position than strangers. They must exercise their own judgment as to the value of what they buy. * * *

"The second principle is that where persons form such an association, or begin or start the project of one, from that time they do stand in a confidential relation to each other, and to all others who may subsequently become members or subscribers, and it is not competent for any of them to purchase property for the purposes of such a company and then sell it at an advance without a full disclosure of the facts. They must account to the company for the profits, because it legitimately is theirs."

In another case,[1] where there were actual misrepresentations, it was said: "If, in order to get up a company, they represented themselves as having acted for the association to be formed, and proposed to sell at the same prices they paid, and their purchases were taken on these representations, and stockholders invested in reliance upon them, it would be a fraud on the company and all those interested, to allow them to retain the large profits paid them by the company in ignorance of the true sums actually advanced."

In this case the defendants were subscribers with others to the stock of a projected company, and after the plan had been formed, secured to themselves an option upon the property, which they afterwards sold to the company at a greatly advanced price.

A promoter is not required to account for profits arising from a sale of land to a corporation at an advance of the price paid for it by him where a notice was attached to all the subscription papers to the effect that he had an option and would sell the land to the corporation for a specified amount and no representations were made as to the amount he had paid for it.[2]

[1]Simons v. Vulcan Oil Co., 61 Pa. St. 202, 217.

[2]Richardson v. Graham (W. Va.), 30 S. E. Rep. 92.

§ 55. **Personal liability of promoters on contracts.**—When promoters assume to contract in the name of a corporation not in being they, upon well understood principles of law, become liable individually upon such contracts. This is true in all cases unless the creditor expressly waives his rights against the promoters and agrees to look to the future corporation for the payment of his debt.[1] The intention of the creditor in such a case is always a question of fact, and is properly submitted to a jury.[2] An express agreement with the promoters that the creditor will look to them alone for payment inures to the benefit of the corporation when organized, and it is therefore not liable upon the contract, although its charter contains an express provision that it shall be liable for such debts when incurred in connection with its organization.[3]

§ 56. **Liability to subscribers whose subscriptions are obtained by fraud.**—The promoters of a corporation are liable in damages to subscribers for stock whose subscriptions are obtained by fraud.[4] Under the English statute every contract relating to the formation of a corporation or to its capital, property or business, when formed; or to the position pecuniary or otherwise in regard to the company or its promoters or vendors; or of the directors or other officers of the company, which may affect the judgment of a person invited to take shares, must be disclosed, if one of the parties to the contract is, at the date of the contract, or subsequently becomes, a director, promoter or trustee of the company.[5] Hence, where the owner of property agreed to sell it to a company for a stipulated amount, but by a series of contracts it was arranged that only

[1]Carmody v. Powers, 60 Mich. 26, 26 N. W. Rep. 801. See Morton v. Hamilton College (Ky.), 35 L. R. A. 275; Shields v. Clifton Hill, etc., Co., 94 Tenn. 123, 26 L. R. A. 509; Walton v. Oliver, 49 Kan. 107, 30 Pac. Rep. 172; Hersey v. Tully, 8 Colo. App. 110, 44 Pac. Rep. 854; Roberts, etc., Co. v Schlick, 62 Minn. 332, 64 N. W. Rep. 826. See articles in 16 Am. Law Rev. 281 and 671.

[2]Higgins v. Hopkins, 3 Exch. (W. H. & G.) 163.

[3]Savin v. Hoylake R. Co., L. R., 1 Exch. 9.

[4]Miller v. Barber, 66 N. Y. 558; Paddock v. Fletcher, 42 Vt. 389.

[5]Statement of rule in 7 Eng. Rul. Cas. 497.

a small portion of this sum should be retained by them, and the balance divided among the promoters, and the prospectus did not disclose these contracts, and the plaintiffs subscribed for shares without knowledge of the facts, they were allowed to recover the value of the shares, for which they subscribed, from the promoters.[1]

§ 57. **Fraudulent prospectus.**—One who is induced to subscribe for stock in a corporation by fraudulent representations contained in a prospectus issued by the promoters of a corporation may recover the resulting damages from the promoters. In England the original allottee of shares alone is entitled to maintain the action. But a purchaser from an original allottee may recover damages caused by misrepresentations in the prospectus, if he can show that the prospectus was intended by those issuing it to be, and was in fact, communicated to him prior to his purchase of the shares. The rule is founded upon the theory that when the allotment was completed the office of the prospectus was exhausted, and that a person who had not become an allottee, but was a subsequent purchaser of shares in the market, was not so connected with the prospectus as to render those who had issued it liable to indemnify him against the losses which he had suffered in consequence of the purchase.[2] Under the American decisions when directors or promoters of a corporation knowingly issue or sanction the circulation of a false prospectus, containing untrue statements of material facts, the natural tendency of which is to deceive and mislead the community, and to induce the public to purchase its stock, they are responsible to those who are injured thereby.[3] Judge Thompson, after criticising the rule of Peek v. Gurney, says:[4] "It is a subject of congratulation that a doctrine so plainly destitute of any foundation in reason,

[1]Sullivan v. Metcalfe, 5 C. P. D. 455, 7 Eng. Rul. Cas. 497.

[2]Peek v. Gurney, L. R., 6 H. L. 377; Scott v. Dickson, 29 L. J. Ex. 62; Derry v. Peek, 14 App. Cas. 337.

[3]Morgan v. Skiddy, 62 N. Y. 319; Cross v. Sackett, 2 Bosw. 617 (N. Y.).; Watson v. Crandall, 7 Mo. App. 233, 78 Mo. 583; Bruff v. Mali, 36 N. Y. 200; Cazeaux v. Mali, 25 Barb. 578 (N. Y.).

[4]Thompson Corp., II, § 1472.

and so opposed to common opinions of justice and business morality, has not obtained a foothold in this country. We follow the doctrine of the overruled decisions in England, and hold that it is not necessary in order to support such an action, that the false representations were made directly to the plaintiff. It will be sufficient if they were contained in circulars, prospectuses, or other advertisements, with a view of influencing the public at large, or any member of the public, who might be influenced by them to purchase shares; and that the plaintiff saw them, and on the faith of the statements contained in them became a purchaser of shares. * * * It is not necessary that the representations should have been communicated directly to the persons thereby induced to purchase the shares. Nor is it necessary that they should have been concocted with a view of deceiving those particular persons; it is sufficient that they were concocted with a view of deceiving any person whom the deception might catch and impose upon."

§ 58. **Liability of corporation on contracts made by promoters.**—As a general rule a corporation is not liable on the contracts of its promoters, and parties who have contracted with them in the name of the corporation have no right of action against it unless the engagement made on its behalf is subsequently adopted by it.[1] No relation of agency can exist between the promoter and a principal not in existence. The rule of non-liability is not affected by the fact that the pro-

[1] Munson v. Syracuse R. Co., 103 N. Y. 58; Gent v. Mfg., etc., Co., 107 Ill. 652; Western, etc., Co. v. Consley, 72 Ill. 531; Weatherford v. Railway Co., 86 Tex. 350; Carey v. Mining Co., 81 Iowa 674, 47 N. W. Rep. 882; Standard, etc., Co. v. Dem., etc., Co., 87 Wis. 127, 58 N. W. Rep. 238; Battelle v. N. W., etc., Co., 37 Minn. 89; McArthur v. Times, etc., Co., 48 Minn. 319; Davis v. Ravenna, etc., Co., 48 Neb. 471, 67 N. W. Rep. 436; Buffington v. Bardon, 80 Wis. 635; San Joaquin, etc., Co. v. West, 94 Cal. 399; Pittsburgh, etc., Co. v. Quintrell, 91 Tenn. 693; Winters v. Hub, etc., Co., 57 Fed. 287. A contract to offer stock to the corporation at the lowest price at which the holder is willing to sell, before offering it to any other purchaser, is not binding in favor of the corporation when it was made by proposed stockholders before the corporation was in existence as a legal entity. Ireland v. Globe, etc., Co. (R. I.), 38 Atl. Rep. 116, 38 L. R. A. 299.

moters become the sole stockholders of the corporation.[1] A corporation is not responsible for representations made by its promoters.[2]

§ 59. **Adoption of contract by corporation.**—No rights, legal or equitable, arise in favor of a corporation in respect of transactions, whether complete or inchoate, merely because entered into in contemplation of the creation of such corporation.[3] But if the corporation has the power to enter into such a contract, it may adopt the contract made in its name by the promoters, and thus bind itself to its performance. It then becomes liable by virtue of the act of adoption, and not upon the theory of the agency of the promoters. It does not, strictly speaking, ratify the acts of the promoters, as ratification implies an existing principal; it enters into a new contract, which dates from the time of the act of adoption.[4] The act of adopting the contract must be attended by the formalities necessary to the making of an original contract. Thus, if the use of a seal or a resolution of the board of directors is necessary to the making of such a contract, it is necessary when the corporation adopts a contract made by a promoter for it. Under ordinary circumstances the adoption of the agreement may be shown by acts of acquiescence on the part of the corporation or its authorized agents.[5] The president or general manager of

[1]Battelle v. N. W., etc., Co., 37 Minn. 89. But see Paxton v. Bacon, etc., Co., 2 Nev. 259 (New ed.), 768.

[2]Oldham v. Mt. Sterling, etc., Co. (Ky.), 45 S. W. Rep. 779.

[3]Plaquemines, etc., Co. v. Buck, 52 N. J. Eq. 219, 24 Atl. Rep. 1094.

[4]Richardson v. Graham (W. Va.), 30 S. E. Rep. 92; McArthur v. Times, etc., Co., 48 Minn. 319; Huron, etc., Co. v. Kittleson, 4 S. Dak. 520; Weatherford v. R. Co., 86 Tex. 350, 24 S. W. Rep. 795; Reichwald v. Commercial Hotel, 106 Ill. 439.

That the corporation can not be charged by virtue of the technical doctrine of ratification, which applies only to acts performed on behalf of an existing principal, see also Caledonia, etc., Co. v. Helensburg, etc., Trustees, 2 Macq. H. L. Cas. 391, 409; Oakes v. Cattaraugus, etc., Co., 143 N. Y. 430; dissenting opinion, Melhado v. Porto Alegre, etc., R. Co., L. R. 9 C. P. 503. It is sometimes said that there may be a ratification. See Oakes v. Cattaraugus, etc., Co., 143 N. Y. 430, and note 26 L. R. A. 546.

[5]Oakes v. Cattaraugus, etc., Co., 143 N. Y. 430, 26 L. R. A. 544.

a corporation may adopt a contract made by himself for the corporation before it was legally created which he would have power to make at the time of the adoption.[1] An adoption procured by the active co-operation of directors who have a private interest in the contract does not bind the corporation.[2] In Massachusetts it is held that a corporation can not become a party to a contract made in its name by promoters before the organization of the corporation, even by adoption.[3]

§ 60. **Acceptance of benefits under the contract.**—A corporation may become liable on a contract made by its promoters by reason of acts which create an estoppel. If it accepts the benefits which accrue under the contract, it can not escape responsibility for the burdens.[4] Thus where the promoters agreed on behalf of a railway company that if a bonus was given, the road would be constructed between certain points, and that coal would be carried at a stipulated rate, it was held that by accepting the bonus the company was bound to com-

[1] Battelle v. N. W. Cement Co., 37 Minn. 89; Burden v. Burden, 40 N. Y. Sup. 499; Schreyer v. Mills Co., 29 Ore. 1, 43 Pac. Rep. 719.

In Ireland v. Globe, etc., Co. (R. I.), 38 Atl. Rep. 116, 38 L. R. A. 299, it was held that the mere issue of certificates of stock by a corporation is not a ratification of a contract made before it came into existence, between the proposed incorporators to the effect that they would not transfer their shares without giving the company an option to purchase them.

[2] Munson v. Syracuse, etc., R. Co., 103 N. Y. 58.

[3] Abbott v. Hapgood, 150 Mass. 248, 22 N. E. Rep. 907; Penn, etc., Co. v. Hapgood, 141 Mass. 145, 7 N. E. Rep. 22.

[4] Chicago, etc., Co. v. Creamery Co. (Ga.), 31 S. E. Rep. 809; Weatherford, etc., R. Co. v. Granger, 86 Tex. 350, 24 S. W. Rep. 795; Paxton, etc., Co. v. First National Bank, 21 Neb. 621, 33 N. W. Rep. 271; Grape, etc., Co. v. Small, 40 Md. 395; Moore, etc., Co. v. Towers, etc., Co., 87 Ala. 206, 6 So. Rep. 41; Frankfort, etc., Co. v. Churchill, 6 T. B. Mon. 427, 17 Am. Dec. 159. In Morton v. Hamilton College (Ky.), 38 S. W. Rep. 1, 35 L. R. A. 275, it was held that promoters of an incorporated college who advance money or assume an obligation to pay the interest on one of the subscriptions to a fund for the purchase of property of the college, when to do this it is necessary to obtain the subscription, and it is done at the request of some and with the consent of all of those acting as trustees of the prospective corporation, on the understanding that the college will repay them or save them harmless, can recover from it the amount of such interest which they have been compelled to pay and which went into the fund used in buying the college property.

ply with the terms of the contract.[1] So where a number of persons not incorporated, but associated for a common object, intending to procure a charter, authorize acts to be done in furtherance of their object by one of their number, with the understanding that he should be compensated, it was held that if such acts were necessary to the organization, and were accepted by the corporation and the benefits thereof enjoyed, they must be taken with the burden. The court said: "If the body for whom the projectors assumed to act does come into existence, it can not take the benefits of the contract without performing that part of it which the projectors undertook that it should perform."[2]

Where, after the execution of articles of incorporation and the selection of officers, but before the filing and recording of the articles, and before the time fixed by the articles for commencing business, the president in the name of the corporation executed a promissory note in payment for certain property which after the perfecting of the corporation came into the possession of the corporation as its property and continued to be used by it as such, the corporation is liable on the note. The court said: "The conclusion is inevitable, granting the entire want of power on the part of the officers, or promoters of the corporation to act as such at the date of the note, that the retaining possession of the consideration by the corporation after its organization is a ratification of the contract with all its terms and obligations."[3]

§ 61. **Limited to obligations of the accepted contract.**—The acceptance of the contract entered into by the promoters imposes upon the corporation liability only for the obligations which grow out of the contract. "When it is said that when a corporation accepts the benefit of a contract made by its promoters, it takes it *cum onere*, it is important to understand distinctly what is meant. There is, so far as this matter is con-

[1] Weatherford, etc., R. Co. v. Granger, 86 Tex. 350, 24 S. W. Rep. 795, Wilgus' Cases; Burrows v. Smith, 10 N. Y. 550.

[2] Bell, etc., R. Co. v. Christy, 79 Pa. St. 54.

[3] Paxton Cattle Co. v. First Nat'l Bank, 21 Neb. 621, 33 N. W. Rep. 271.

cerned, a radical difference between a promise made on behalf of the future corporation in the contract itself, the benefits of which the corporation has accepted, and the promise in a previous contract to pay for services in procuring the latter to be made.'' Hence, where a proposition was made on behalf of the company by its promoters that if a bonus should be subscribed and paid to it, it would build its road between certain points, and would carry coal at a certain stipulated rate, by accepting the bonus the company became bound to fulfill the stipulations of the contract. But where it appeared that one of the promoters promised the plaintiff that if he would assist in procuring subscribers to the bonus, the company would pay him for his services, this was no part of the contract the benefits of which were taken by the company. Hence, by accepting the contract, the company did not become liable for such services.[1]

§ 62. **The expenses and services of promoters.** — The great weight of authority supports the rule that corporations are not liable for expenses incurred or services rendered in the organization of the corporation unless made so by statute or by its charter.[2] But it has been held that where the corporation accepts the benefit of the services legitimately rendered or of expenses incurred before its organization, and which were necessary for its organization, it is estopped to deny liability therefor.[3] In such case the services must have been necessary and reasonable, and rendered with the understanding that they should accrue to the benefit of the corporation, and with the expectation that they would be paid for by it.[4] The liability rests upon a promise implied by law from the fact that the corporation, after it had capacity to contract, accepted the benefits, and therefore must be deemed to have taken the burdens at the

[1] Weatherford, etc., R. Co. v. Granger, 86 Tex. 351, 24 S. W. Rep. 795.

[2] Rockford, etc., R. Co. v. Sage, 65 Ill. 328, 16 Am. R. 587; N. Y. & N. H. R. Co. v. Ketchum, 27 Conn. 170; Re Rotherham Alum Co., L. R. 25 Ch. Div. 103; Davis, etc., Co. v. Hillsboro, etc., Co., 10 Ind. App. 42.

[3] Low v. Conn., etc., R. Co., 45 N. H. 370.

[4] Perry v. R. Co., 44 Ark. 383; West Point, etc., Co. v. Rose (Miss., May 23, 1898), 23 So. Rep. 629.

same time, and is estopped to show want of capacity to make the contract. This rule practically renders a corporation liable in all cases for services and expenses rendered in its organization, which it necessarily accepts by existing.

Where services are rendered at the request of all the corporators, and after incorporation no outside persons or capital are taken in, it is held that the corporation may be liable in equity for the value of such services. "Under such circumstances the property of no one but those who contracted the debts and were originally liable, would be taken or subjected to the payment of it. The same persons continue the same business with the same property with no substantial change except in name. In such a case there is no reason why in equity the corporation should not be primarily liable for the debts, as it has succeeded to the property of the association." But this rule does not apply where third persons join the corporation.[1]

IV. Corporations as Persons and Citizens.

§ 63. **The citizenship of a corporation.**—For the purposes of jurisdiction a corporation is taken to be a citizen of the state by which it was created.[2] The theory that the corporate person has a residence in the land of its birth without reference to its constituent parts controls the decision in many cases. But the supreme court of the United States bases its decisions upon the presumption that all of the stockholders of a corporation are citizens of the state which created the corporation. Originally this presumption was one of fact and the subject of allegation and traverse, which permitted the jurisdiction of the federal courts to be defeated by showing the actual residence of the stockholders. But after a long contest, it is settled that the presumption of citizenship is one of law, which can not be overthrown by evidence.[3] "Strictly

[1]Paxton v. Bacon Mill Co., 2 Nev. 258; Ritchie v. McMullen, 79 Fed. Rep. 523 (C. C. A.), 64 Fed. Rep. 253.

[2]Shaw v. Quincy Min. Co., 145 U. S. 444; Nashua R. Co. v. Lowell R. Co., 136 U. S. 356; S. S. Co. v. Tugman, 106 U. S. 118; Connor v. Vicksburg R. Co., 36 Fed. Rep. 273, 1 L. R. A. 331; St. Louis, etc., R. Co. v. Newcom, 6 C. C. A. 172, Ann.

[3]St. Louis, etc., R. Co. v. James, 161 U. S. 545, Wilgus' Cases; Muller v Dows, 94 U. S. 444.

speaking,'' says Judge McCrary,[1] "corporations can not be citizens; and, therefore, in order to hold them amenable to the federal jurisdiction on the ground of citizenship, it has been found necessary to assume, often contrary to the fact, that all the stockholders are citizens of the state by which the corporations are created. It is only by virtue of this assumption that a corporation can be said to be a citizen of any state. The presumption that all the stockholders are citizens of the state under whose laws they incorporate is a conclusive presumption, and the facts will not be inquired into.''

§ 64. **Incorporation in several states.**—It is not uncommon for several states to incorporate what to all intents and purposes is the same corporation. It is impossible, however, for a state to give extraterritorial force to its laws.[2] And, hence, although bearing the same name, there are as many corporations as there are creating states.[3] For purposes of jurisdiction the corporation is a corporation of each state, and when acting in either of the states it acts under the authority of the charter from that state.[4] Subject to constitutional limitations, a legislature has entire control over the matter of creating corporations, and may thus provide a method by which a foreign corporation may become a domestic corporation. A corporation, as chartered in a foreign state, may thus be made a domestic corporation.[5] "It is not true that one state may not

[1]Pac. R. Co. v. Mo. Pac. R. Co., 23 Fed. Rep. 565.

As the jurisdiction rests upon the citizenship of the parties, a pleading must allege the state by which the corporation was created, and this must be a foreign state. No averment of citizenship of the stockholders is permitted.

LaFayette Ins. Co. v. French, 18 How. (U. S.) 404; B. & O. R. Co. v. Harris, 12 Wallace (U. S.) 65; St. Louis, etc., R. Co. v. Newcom, 56 Fed. Rep. 951, 6 C. C. A. 172.

[2]Rece v. Newport News R. Co., 32 W. Va. 164, 3 L. R. A. 572.

[3]Mo. Pac. R. Co. v. Meeh, 69 Fed. Rep. 753, 30 L. R. A. 250; Bridge Co. v. Woolley, 78 Ky. 523; Louisville, etc., R. Co. v. N. A. & C. R. Co., 75 Fed. Rep. 433; R. Co. v. Roberson, 61 Fed. Rep. 592; Nashua, etc., Corp. v. Boston, etc., Corp., 136 U. S. 356.

[4]Quincy Bridge Co. v. Adams, 88 Ill. 615.

[5]Stout v. R. Co., 8 Fed. Rep. 794; James v. R. Co., 46 Fed. Rep. 47. A railroad corporation chartered by one state becomes a domestic corporation of another state by acquiring by consolidation the property and franchises of two domestic railway corporations

incorporate a corporation of another state as such. It may be done, too, without any specific provisions for the stock or internal government of the new corporation.'"[1] When a corporation is created out of a corporation of another state, the indisputable presumption of citizenship of the members which arises when the corporators are individuals does not apply; and the new corporation for purposes of Federal jurisdiction is regarded as a citizen of the same state as that of the constituent corporation.[2]

§ 65. **Citizenship within the fourteenth amendment.**—A corporation is not a citizen of the United States within the meaning of all the provisions of the constitution of the United States; but it is a *person* within the meaning of the clause in § 1 of the fourteenth amendment to the constitution, which forbids a state to deny to any persons in its jurisdiction the equal protection of the laws.[3] A statute of Tennessee which gave to residents of that state priority over non-residents in the distribution of the assets of a foreign corporation, which, by filing its articles of association in the state, became a domestic corporation, was held unconstitutional, in so far as it discriminated against citizens of other states.[4] "But it is equally well settled," said Mr. Justice Harlan, "and we now hold that a corporation is not a citizen within the meaning of the constitutional provision that 'the citizens of each state shall be entitled to all privileges and immunities of citizens in the several states.' * * * Since, however, a corporation is a 'per-

of the latter state. Bradley v. Ohio, etc., R. Co., 78 Fed. Rep. 387, 119 N. C. 718.

[1]Louisville, etc., R. Co. v. Ry. Co., 75 Fed. Rep. 433; Clark v. Barnard, 108 U. S. 436; Graham v. Ry. Co., 118 U. S. 161; Railway Co. v. Roberson, 61 Fed. Rep. 592.

[2]Railway Co. v. James, 161 U. S. 545.

[3]Santa Clara County v. South. Pac. R., 118 U. S. 394; Pembina, etc., Co. v. Pa., 125 U. S. 187; Mo. Pac. R. Co. v. Mackey, 127 U. S. 205; M. & St. L. R. Co. v. Beckwith, 129 U. S. 26; Covington, etc., Co. v. Sanford, 164 U. S. 592; Smythe v. Ames, 169 U. S. 522; Hammond, etc., Co. v. Best, 91 Me. 431, 42 L. R. A. 528. But the fourteenth amendment does not destroy the police power of the state. See note to State v. Goodwill, 25 Am. St. Rep. 870–890.

[4]Blake v. McClung, 172 U. S. 239, Wilgus' Cases. The chief justice and Mr. Justice Brewer dissenting.

son' within the meaning of the fourteenth amendment * * * may not the Virginia corporation invoke for its protection the clause of the amendment declaring that no state shall deprive any person of property without due process, nor deny to any person within its jurisdiction the equal protection of the laws? We are of opinion that this question must receive a negative answer. Although this court has adjudged that the prohibitions of the fourteenth amendment refer to all the instrumentalities of the state, to its legislative, executive, and judicial authorities, it does not follow that within the meaning of that amendment the judgment below deprived the Virginia corporation of property without due process of law, simply because its claim was subordinated to the claims of the Tennessee creditors. That corporation was not, in any legal sense, deprived of its claim, nor was its right to reach the assets of the British corporation in other states or countries disputed. It was only denied the right to participate upon terms of equality with Tennessee creditors in the distribution of particular assets of another corporation doing business in that state. It had notice of the proceedings in the state court, became a party to those proceedings, and the rights asserted by it were adjudicated. If the Virginia corporation can not invoke the protection of the second section of article four of the constitution of the United States relating to the privileges and immunities of citizens in the several states, as its co-plaintiffs in error have done, it is because it is not a citizen within the meaning of that section; and if the state court erred in its decree in reference to that corporation, the latter can not be said to have been thereby deprived of its property without due process of law within the meaning of the constitution.

"It is equally clear that the Virginia corporation can not rely upon the clause declaring that no state shall 'deny to any person within its jurisdiction the equal protection of the laws.' * * * Without attempting to state what is the full import of the words, 'within its jurisdiction,' it is safe to say that a corporation not created by Tennessee, nor doing business there under conditions that subjected it to process issuing from the

courts of Tennessee at the instance of suitors, is not, under the above clause of the fourteenth amendment, within the jurisdiction of that state. Certainly, when the statute in question was enacted the Virginia corporation was not within the jurisdiction of Tennessee. * * * We adjudge that the statute, so far as it subordinates the claims of private business corporations not within the jurisdiction of the state of Tennessee (although such private corporations may be creditors of a corporation doing business in the state under the authority of that statute), to the claims against the latter corporation, of creditors residing in Tennessee, is not a denial of the 'equal protection of the laws' secured by the fourteenth amendment to persons within the jurisdiction of the state, however unjust such a regulation may be deemed."

§ 66. **A corporation as an "inhabitant" of a state.**—The weight of authority establishes a distinction between the citizenship and inhabitancy of a corporation, at least if an *alien* corporation.[1] Although a corporation is a *citizen* only of the state by which it is created, if an alien corporation it may for certain purposes be considered an *inhabitant* of a state where it has its principal place of business. Under the statute which provides that except when "the jurisdiction is founded only on the fact that the action is between citizens of different states, no civil suit shall be brought * * * against any person by original process or proceeding in any other district than that whereof it is an inhabitant," it has been held in the lower United States courts that a corporation is an inhabitant of the place in which it has its principal place of business, and where it keeps its records and holds its corporate meetings. These holdings were made under the provisions of the Revised Statutes of 1875, when the word "inhabitant" was followed by "or that in which he was found." Since the latter words are not in the law as amended in 1888, it is held that a corporation

[1] United States v. Southern Pac. R. Co., 49 Fed. Rep. 297; East Tennessee R. Co. v. Insurance Co., 49 Fed. Rep. 608; Gilbert v. Insurance Co., 49 Fed. Rep. 884; In re Hohorst, 150 U. S. 653.

is an inhabitant only of the state and district in which it is incorporated.[1]

§ 67. **Place of doing business—License—Effect on citizenship.**—As a corporation is a creature of local law it does not change its citizenship by extending its business into other states.[2] A foreign corporation does not by filing its articles of incorporation in another state as required by the laws of that state, lose its status as a foreign corporation.[3] This is also true where a corporation goes into another state and there purchases and operates a line of railways.[4] Where a corporation has the right to sell its railroad to a company incorporated by another state, under a law which provides that the purchasing company shall have "all the rights and privileges" of the vendor, the purchasing company does not acquire the citizenship of the vendor company.[5] The granting of a license to a corporation to do business in another state does not make it a citizen of that state. Thus, a Maryland corporation was authorized to do business in Virginia under an act which declared "that the same rights and privileges shall be, and are hereby granted to the aforesaid company within the territory of Virginia, and the said company shall be subject to the same pains, penalties and obligations as are imposed by said act, and the same rights, privileges and immunities, which are reserved to the state of Maryland as to the citizens thereof, are hereby reserved to the state of Virginia and her citizens." The act was construed as granting a license only, and therefore as not making the corporation a Virginia corporation.[6] In a case where it appeared that an existing railroad corporation was authorized by the laws of a state other than that by which it was created to ex-

[1] Gormully, etc., Co. v. Pope Mfg. Co., 34 Fed. Rep. 818; Filli v. Railway Co., 37 Fed. Rep. 65. But see Riddle v. Railway Co., 39 Fed. Rep. 290; In re Keasby & M. Co., 160 U. S. 221.

[2] B. & O. R. Co. v. Koontz, 104 U. S. 5.

[3] Chicago, etc., R. Co. v. Minn., etc., R. Co., 29 Fed. Rep. 337.

[4] B. & O. R. Co. v. Koontz, 104 U. S. 5; R. Co. v. Cary, 28 Ohio St. 208.

[5] Morgan v. E. Tenn. R. Co, 48 Fed. Rep. 705; St. Louis, etc., R. Co. v. Newcom, 2 C. C. A. 174, Ann.

[6] B. & O. R. Co. v. Harris, 12 Wall. 65.

tend its road into such state, Mr. Justice Miller said:[1] "It may not be easy in all such cases to distinguish between the purpose to create a new corporation which shall owe its existence to the law or statute under consideration, and the intent to enable the corporation already in existence under laws of another state to exercise its functions in the state where it is so received. * * * To make such a company a corporation of another state, the language used must imply creation or adoption in such form as to confer the power usually exercised over corporations by the state, or by the legislature, and such allegiance as a state corporation owes to its creator. The mere grant of privileges or powers to it as an existing corporation, without more, does not do this, and does not make it a citizen of the state conferring such powers." And even where the statute provided that upon filing a certified copy of its articles of association, by a foreign railroad company, with the secretary of state, it should become a corporation of Arkansas, it was held that compliance with such statute, and leasing, purchasing and operating a railroad in Arkansas, did not make it a citizen of Arkansas within the meaning of the federal constitution.[2]

§ 68. **A corporation as a person.**[3]—Corporations are to be deemed persons within the meaning of statutes when the circumstances in which they are placed are identical with those of natural persons who are expressly included within the operation of the statutes.[4] They are within the meaning of statutes using such words as person and inhabitant when they come within the reason and purport of the statutes.[5] Generally, a statute will be held to include corporations, unless there is something in the statute tending to show that it is intended to be re-

[1] Penn. Co. v. St. Louis, etc., R. Co., 118 U. S. 290.

[2] St. Louis, etc., R. Co. v. James, 161 U. S. 545, Wilgus' Cases.

[3] See Wilgus' Cases, Corporation as a Person, and note.

[4] Crafford v. Supervisors, 87 Va. 110, 10 L. R. A. 129; Beaston v. Farmers' Bank, 12 Peters (U. S.) 102.

[5] People v. Utica, etc., Co., 15 Johns. 358; Proprietors v. Ipswich, 153 Mass. 42, 26 N. E. Rep. 239; Denny, etc., Co. v. Schram, 6 Wash. 134.

stricted in its application to natural persons.[1] Corporations are persons within the meaning of statutes relating to taxation, unless a contrary intent appears.[2] So a foreign corporation is a person within the statute relating to the limitation of actions.[3] Statutes which prohibit persons from engaging in banking,[4] or provide that all persons shall be liable for injuries which result in death;[5] or that all inhabitants or residents shall pay taxes;[6] that testimony shall be admitted as against certain persons;[7] that all persons may do certain acts in relation to promissory notes, apply to corporations.[8] The term "persons," when used in attachment and garnishment statutes, includes corporations when they are placed in a position identical with that of natural persons.[9] The words "debtor" and "creditor," used in a statute giving a remedy by attachment, include corporations.[10]

[1] Stribfling v. Bank, 5 Rand. (Va.) 132.

[2] British, etc., Co. v. Comm'rs, 31 N. Y. 32.

[3] Alcot v. Tioga R. Co , 20 N. Y. 210.

[4] People v. Utica, etc., Co., 15 Johns. 358.

[5] South v. Paulk, 24 Ga. 356.

[6] Bank v. Deveaux, 5 Cranch 61.

[7] LaFarge v. Exchange, etc., Co., 22 N. Y. 352.

[8] State v. Waram, 6 Hill (N. Y.) 33.

[9] B., etc., R. Co. v. Gallahue, 12 Grat. (Va.) 655, 65 Am. Dec. 254; Knox v. Protection, etc., Co., 9 Conn. 430, 25 Am. Dec. 33.

[10] Union Bank v. U. S. Bank, 4 Humph. (Tenn.) 369.

CHAPTER 3.

CORPORATIONS EXISTING WITHOUT LEGAL RIGHT.

§ 69. General statement.
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87. Estoppel limited to *de facto* corporations.
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§ 69. **General statement.**—It has already been stated that there can not be a legal incorporation until there has been a substantial compliance with all the requirements of the statute which are made conditions precedent to incorporation. When such conditions have been thus complied with there results a corporation *de jure* which is able to prove its right to exist as against the direct attack of the state.[1] If, however, there is not substantial compliance with the statutory requirements, there may under certain conditions be a *de facto* corporation, which, except as against the state, is as effective for all practical purposes as a *de jure* corporation. By the great weight of authority, its right to exist and exercise the powers assumed can not be questioned collaterally by a private individual. If

[1] Capps v. Hastings, etc., Co., 40 Neb. 470, 24 L. R. A. 259, Wilgus' Cases.

the state chooses to waive any of the conditions, it can do so, and on grounds of public policy no one else can successfully question the validity of incorporation.

§ 70. **Manner of raising the question of corporate existence.**—If a pretended corporation is neither *de jure* nor *de facto*, it has no standing, and its corporate existence may be questioned collaterally by the state or by an individual, at least when there is no reason for an estoppel.[1] The right to exercise the franchise of being a corporation can be called in question only by proceedings in the nature of *quo warranto* instituted by the state.[2] This rule applies to corporations organized under general laws, and to those created by special charter.[3] "Where the law authorizes a corporation, and there is an effort in good faith to organize the corporation under the law, and thereafter, as a result of such effort, corporate functions are assumed and exercised, the organization becomes a corporation *de facto*, and as a general rule, the legal existence of such a corporation can not be inquired into collaterally, although some of the required legal formalities may not have been complied with. Ordinarily such an inquiry can only be made in a direct proceeding in the name of the state, and no private persons having dealings with a *de facto* corporation can be permitted to say that it is not also a corporation *de jure*."[4] This rule is held to have no application where in-

[1]Martin v. Deetz, 102 Cal. 55; Childs v. Hurd, 32 W. Va. 66, 9 S. E. Rep. 362; Att'y-Gen. v. Hanchett, 42 Mich. 436.

Only the state can claim that the charter of a *de facto* corporation is void because unconstitutional. Taylor v. Portsmouth, etc., R. Co. (Me.), 39 Atl. Rep. 560; Dubs v. Egli, 167 Ill. 514, 47 N. E. Rep. 766; Smith v. Mayfield, 163 Ill. 447.

[2]Andrews v. Nat., etc., Works, 46 U. S. App. 281, 619, 36 L. R. A. 139; Paulino v. Portuguese, etc., Assn., 18 R. I. 165; John V. Farwell Co. v. Wolf (Wis.), 70 N. W. Rep. 289; E. Norway, etc., Church v. Froislie, 37 Minn. 447, and cases cited in the following notes.

[3]Stout v. Zulick, 48 N. J. L. 599; Wood v. Wiley, etc., Co., 56 Conn. 87.

[4]Andes v. Ely, 158 U. S. 312; Hasselman v. Mfg. Co., 97 Ind. 365; North v. The State, 107 Ind. 356, 8 N. E. Rep. 159; Hamilton v. Railroad Co., 144 Pa. St. 31. See the review of authorities by Mr. Justice Marshall in dissenting opinion in Bergeron v. Hobbs, 96 Wis. 641, 71 N. W. Rep. 1056.

dividuals sued for services alleged to have been rendered them personally, deny personal liability, and allege the existence of a corporation to which the services were rendered.[1] As long as irregularities in the matter of organization are overlooked by the state, it is settled by the great weight of modern authority that an individual can not successfully object. This principle applies to a *de facto* foreign corporation as well as to a *de facto* domestic corporation.[2]

§ 71. **Collateral attack upon de facto corporation, and the doctrine of estoppel.**—The courts sometimes fail to distinguish the principle which prevents an individual from questioning the right of a corporation to exist and exercise its franchises[3] from the doctrine of estoppel, which prevents one who has dealt with a *de facto* corporation from questioning its corporate existence *in the particular case* under consideration. In discussing this question the supreme court of Minnesota said:[4] "Under the view we take of the case, it is wholly unnecessary to consider any of these questions. The plaintiffs are at least corporations *de facto*. Such a corporation, at least where there is a law under which a corporation might have been legally formed with such power, is capable of taking and holding property as grantee, as well as a corporation *de jure*, and conveyances to it are valid as to all the world except the state in proceedings in *quo warranto*, or other direct proceedings to inquire into its right to exercise corporate franchises. And in an action by it to recover such property, no private person will be allowed to inquire collaterally into the regularity of its organization. This rule *is not founded upon any principle of estoppel, as is sometimes assumed*, but upon the broader principles of common justice and public policy. It would be unjust and intolerable if, under such circumstances, every interloper

[1]Owen v. Shepard, 8 C. C. A. 244, 59 Fed. Rep. 746.

[2]Wright v. Lee, 4 S. D. 237, 55 N. W. Rep. 931; Lancaster v. Amsterdam Imp. Co., 140 N. Y. 576, 35 N. E. Rep. 964.

[3]Andrew v. National, etc., Works, 46 U. S. App. 281, 619, 36 L. R. A. 139, 153.

[4]Trustees, etc., v. Froislie, 37 Minn. 447. See language of Brewer, J., in Pape v. Capital Bank, 20 Kan. 440.

and intruder were allowed to take advantage of every informality or irregularity of organization."

In considering the same question, the supreme court of Ohio said :[1] "The theory that a *de facto* corporation has no real existence, that it is a mere phantom, to be invoked only by that rule of estoppel which forbids a party who has dealt with a pretended corporation to deny its corporate existence, has no foundation either in reason or authority. A *de facto* corporation is a reality. It has an actual and substantial legal existence. It is, as the term implies, a corporation."

I. De Facto Corporations.

§ 72. **Definition.**—A *de facto* corporation is an apparent corporate organization asserted to be a corporation by its members and actually existing as such, but lacking the creative fiat of the state.[2] It is a fact, and not a mere figment of the legal imagination. Its existence is the result of certain conditions resulting from the acts of its incorporators. A *de facto* corporation exists when, from defect or irregularity in the organization, or from some omission to comply with the conditions precedent, a corporation *de jure* is not created. There must, however, have been a colorable compliance with the requirements of some law under which an association might lawfully be incorporated, for the purpose and with the powers assumed, and a user of the rights claimed to be conferred by the law.[3] While the decisions are not entirely clear,[4] it is evident that three things must exist before there can be a corporation *de facto*. 1. Capacity to become a corporation *de jure*. There must be at the time of its organization a valid law under which a corporation with the powers assumed might

[1] Society Perun v. Cleveland, 43 Ohio St. 481, 3 N. E. Rep. 357, Wilgus' Cases.

[2] Re Gibbs' Estate, 157 Pa. St. 59, 22 L. R. A. 276, Wilgus' Cases.

[3] Snider's Sons Co. v. Troy, 91 Ala. 224, 11 L. R. A. 515, 24 Am. St. Rep. 887; Stout v. Zulick, 48 N. J. L. 599, 7 Atl. Rep. 362; Eaton v. Walker, 76 Mich. 579, 43 N.W. Rep. 638; Johnson v. Schulin (Minn.), 73 N.W. Rep. 147; Finnegan v. Noerenberg, 52 Minn. 239.

[4] See for illustration the case of Bergeron v. Hobbs, 96 Wis. 641, 71 N. W. Rep. 1056, Wilgus' Cases.

lawfully be created. 2. A good faith attempt to form a corporation under such a statute; and, 3. User of the powers and franchises claimed by the organization.

§ 73. **Necessity for a valid law.**—By the weight of authority there can not be a *de facto* corporation unless there is a valid law under which the corporation might have been legally incorporated. "To be a corporation *de facto*, it must be possible to be a corporation *de jure;* and acts done in the former case must be legally authorized to be done in the latter, or they are not protected or sanctioned by the law. Such acts must have an apparent right."[1] An attempt to organize under a void special law may result in a *de facto* corporation if there was a general law under which such a corporation could be organized.[2] There may be a *de facto* corporation resulting from an unsuccessful attempt to consolidate existing corporations. Thus, where the laws authorize the consolidation of corporations of different states, the result of an attempted consolidation may be a *de facto* corporation.[3] A *de facto* corporation can never result from an attempt to organize a corporation in direct violation of a prohibitive statute.[4] An attempt to organize a corporation in one state under a charter granted by another state, does not create a *de facto* corporation.[5]

§ 74. **Good faith attempt to organize.**—There must also be a bona fide attempt to organize a legal incorporation under the statute. "To give a body of men assuming to act as a corporation, where there has been no attempt to comply with the

[1] Evenson v. Ellingson, 67 Wis. 634, 31 N. W. Rep. 342; Eaton v. Walker, 76 Mich. 579, 6 L. R. A. 102; Heaston v. Cincinnati, etc., R. Co., 16 Ind. 275; Abbott v. Omaha, etc., Co., 4 Neb.416; Am., etc., Co. v. Minn., etc., R. Co., 157 Ill. 641, 42 N. E. Rep. 153; Guthrie v. Oklahoma, 1 Okla. 188, 21 L. R. A. 841; Duggan v. Colorado, etc., Co., 11 Colo. 113; Jones v. Aspen, etc., Co., 21 Colo. 263, 29 L. R. A. 143; Society Perun v. Cleveland, 43 Ohio St. 481; Dobson v. Simonton, 86 N. C. 493; Norton v. Shelby Co., 118 U. S. 426.

[2] McTighe v. Macon, etc., Co., 94 Ga. 306, 32 L. R. A. 208.

[3] Continental, etc., Co. v. Toledo, etc., R. Co., 82 Fed. Rep. 642.

[4] McTighe v. Macon, etc., Co., 94 Ga. 306; B. & L. Ass'n v. Chamberlain, 4 S. Dak. 271, 56 N. W. Rep. 897.

[5] Duke v. Taylor, 37 Fla. 64, 31 L. R. A. 484. But see Demarest v. Flack, 128 N. Y. 205, and Lancaster v. Amsterdam Imp. Co., 140 N.Y. 576, holding that one state may grant a charter to non-residents enabling them to organize a valid corporation in the state of their residence.

provisions of any law authorizing them to become such, the status of a *de facto* corporation, might open a door to frauds upon the public. It would certainly be impolitic to permit a number of men to have the status of a corporation to any extent merely because there is a law under which they might become incorporated, and they have agreed among themselves to act, and they have acted as a corporation. * * * "Color of apparent organization under some charter or enabling act" does not mean that there shall have been a full compliance with what the law requires to be done, nor a substantial compliance. A substantial compliance will make a corporation *de jure*. But there must be an apparent attempt to perfect an organization under the law. There being such apparent attempt to perfect an organization, the failure as to some substantial requirement will prevent the body being a corporation *de jure;* but if there be user pursuant to such attempted organization, it will not prevent it being a corporation *de facto*.[1]

§ 75. **User of franchise.**—It is also necessary that there be user of the franchise to be a corporation conferred by the charter or law under which the organization was attempted.[2] Slight evidence of user is sufficient when the other requisites exist.[3] But the acts relied upon to show user *must be in their nature corporate acts* and not such as are perfectly consistent with the conduct of an unincorporated society or partnership.[4]

§ 76. **Organization under unconstitutional statute.**—As an unconstitutional act of the legislature is not a law[5] it logically

[1]Finnegan v. Noerenberg, 52 Minn. 239; Bash v. Mining Co., 7 Wash. 122, 34 Pac. Rep. 464; Williamson v. Kokomo, etc., Ass'n, 89 Ind. 389; Venable v. Ebenezer, etc., Ch., 25 Kan. 177, and cases cited in preceding notes. In Bergeron v. Hobbs, 96 Wis. 641, 71 N. W. Rep. 1056, it was held that because of failure to file the certificate of organization and a copy of the constitution in the office of the register of deeds, the organizers did not become a *de facto* corporation. The overwhelming weight of authority is to the contrary, as pointed out in the exhaustive dissenting opinion of Mr. Justice Marshall.

[2]Martin v. Deetz, 102 Cal. 55; Miami, etc., Co. v. Hotchkiss, 17 Ill. App. 622.

[3]Eaton v. Walker, 76 Mich. 579.

[4]Fredenberg v. Lyon Lake M. E. Ch., 37 Mich. 476.

[5]See an article by the present writer on "The Legislature and the Courts" in Pol Sci. Quarterly, v., p. 233.

follows that the legal status of a company organized under authority assumed to be granted by such an act is the same as one formed when there is no law.[1] This would seem to be the prevailing doctrine, although there are authorities to the contrary.[2]

In a recent case it was said:[3] "We may assume that where the existence of a corporation of a given kind is positively forbidden by law, or *where there is no valid constitutional law authorizing the creation of such a corporation*, it can not exist even as a corporation *de facto*. The rule thus stated does not by any means, however, negative the soundness of the proposition that an organization assuming to be a corporation *de jure*, but, for sufficient reasons, is not so in fact, may be a corporation *de facto*, when it is of such a character that it could under existing laws have full and complete corporate being and powers. * * * Our decision is not based upon the idea that the organization of these railroad companies under unconstitutional charters would make them *de facto* corporations, but upon the idea that the purpose for which they were organized being lawful and proper, if they had obtained charters under the general law and organized under them, which they might have done, they would in substance have done what they actually did; that is, they would have observed about the same forms and requirements in the one case as in the other. * * * If the laws under which they proceeded were not good, they may, in our judgment, avail themselves of the existence of the general law on our statute book, and

[1]Eaton v. Walker, 76 Mich. 579; Burton v. Schildbach, 45 Mich. 504, 8 N. W. Rep. 497; Brandenstein v. Hoke, 101 Cal. 131; Heaston v. R. Co., 16 Ind. 275; Snyder v. Studebaker, 19 Ind. 462; McTighe v. Macon, etc., Co., 94 Ga. 306; Evenson v. Ellingson, 67 Wis. 634; Thomps. Corp., § 505.

[2]Coxe v. State, 144 N. Y. 396, 39 N. E. Rep. 400. See Winget v. Ass'n, 128 Ill. 67, 21 N. E. Rep. 12. A corporation organized under a void law can not enforce a mortgage made to it; but if not organized for an unlawful purpose, a receiver for it can demand in equity an accounting for the debt purporting to be secured by it. Burton v. Scheildbach, 45 Mich. 504.

[3]McTighe v. Macon, etc., Co., 94 Ga. 306, 32 L. R. A. 208. Citing and commenting on McCarthy v. Lavasche, 89 Ill. 270, 31 Am. Rep. 83, Wilgus' Cases; Hudson v. Greenhill, etc., Corp., 113 Ill. 618, and many other cases.

of its terms, at least so far as to enable them to be regarded as *de facto* corporations, because they had done practically what that general law required, though not actually following it nor professing to do so."

§ 77. **Status after expiration of term of existence.**—Where the term of existence of a corporation is definitely determined by the charter or statutes, the better rule is that the corporation is *ipso facto* dissolved by the expiration of the time.[1] From this it follows that after such dissolution there is not even a corporation *de facto*, and the fact of corporate existence can be successfully raised by any one not otherwise estopped.

§ 78. **Collateral attack on the right to exercise a franchise.**—The rule that the right to exercise the franchise of being a corporation can not be collaterally questioned in the suit of an individual does not extend so far as to prevent an individual from questioning the right of a corporation to exercise a particular franchise or power. Thus, where a corporation was granted the franchise of collecting tolls for a certain period or under certain conditions, an individual is not prevented from asserting that the time during which the franchise was to be enjoyed has expired.[2]

[1]Bradley v. Reppell, 133 Mo. 545, 32 S. W. Rep. 645; Dobson v. Simonton, 86 S. C. 494; Kurtz v. Paola, etc., Co., 20 Kan. 397; Grand Rapids, etc., Co. v. Prang, 35 Mich. 400; Sturgess v. Vanderbilt, 73 N. Y. 384; LaGrange, etc., R. Co. v. Rainey, 7 Coldw. (Tenn.) 432. "There is much judicial authority for the proposition that where a corporation is brought to an end by the lapse of time, that is, by the expiration of the distinct limitations of its life in its charter, any further exercise of its corporate powers may be questioned collaterally. The governing principle here is that upon the expiration of the time limited by the charter for the existence of the corporation, its dissolution is complete. The dissolution in such case, it has been said, 'is declared by the act of the legislature itself.' The limited time of existence has expired and no judicial determination of that fact is requisite. The corporation is *de facto* dead." Thompson Corps., § 530. *Contra:* "For the mere exercise of its franchise beyond the period for which it was organized, the state alone can complain." Bushnell v. Machine Co., 138 Ill. 67, 27 N. E. Rep. 596. See comment upon Miller v. Newburgh, etc., Co., 31 W. Va. 836, and St. Louis, etc., Co. v. St. Louis, 84 Mo. 202, in Bradley v. Reppell, 133 Mo. 545, 32 S. W. Rep. 645.

[2]Grand Rapids, etc., Co. v. Prang, 35 Mich. 400.

§ 79. **Fraudulent organization.**—It has been held that where the organization is manifestly a fraud upon the statute a *de facto* corporation is not created. Thus, where citizens of New Jersey went to New York, and attempted to form an organization under the laws of New York for the purpose of doing business in New Jersey, it was held that not even a *de facto* corporation was created.[1] But in New York and Ohio this sort of transaction, unless something more appears, is not considered to be a fraud upon the law.[2] Where the whole purpose of the corporation is to perpetrate a fraud, it will not be considered a *de facto* or a *de jure* corporation as to those defrauded, even though all the statutory forms are followed.[3]

§ 80. **Powers of de facto corporations.**—A *de facto* corporation may legally do every act and thing which the same entity could do were it a *de jure* corporation. As to all the world, except the paramount authority under which it acts and from which it receives its charter, it occupies the same position as though in all respects valid; and even as against the state, except in direct proceedings to arrest its usurpation of power, its acts will be treated as efficacious.[4] It has been held that this rule applies only to the ordinary business transactions of such a business corporation, and that it has no application when the corporation attempts to exercise the power of eminent domain,[5] but there appears to be no valid reason for this distinction, and it is generally held that proof of a *de facto* corporation is sufficient in a proceeding by a railway company to condemn land.[6]

[1] Hill v. Beach, 12 N. J. Eq. 31; Booth v. Wonderly, 36 N. J. L. 250; Elizabethtown, etc., Co. v. Green, 46 N. J. Eq. 118; Empire Mills v. Alston, etc., Co. (Tex.), 15 S. W. Rep. 200. See Lancaster v. Amsterdam, etc., Co., 140 N. Y. 576, and § 550, *infra*. See Demarest v. Flack, 128 N. Y. 205, 28 N. E. Rep. 645.

[2] Second Nat'l Bank v. Hall, 35 Ohio St. 158. See also Wright v. Lee (S.D.), 51 N. W. Rep. 706.

[3] Metcalf v. Arnold, 110 Ala. 180; First Nat'l Bank v. F. C. Trebein Co., 59 Ohio St. 316; Christian, etc., Co. v. Fruitdale, etc., Co. (Ala.), 25 So. Rep 566.

[4] Miller v. Newburgh, etc., Co., 31 W. Va. 836; People v. LaRue, 67 Cal. 530; Bushnell v. Machine Co., 138 Ill. 67, 27 N. E. Rep. 596; Butchers' Bank v. McDonald, 130 Mass. 264; Whitney v. Robinson, 52 Wis. 308, 10 N. W. Rep. 512; Duggan v. Col., etc., Co., 11 Colo. 113.

[5] Atkinson v. Railway Co., 15 Ohio St. 21; Atlantic, etc., Co. v. Sullivant, 5 Ohio St. 276; Miller v. Newburgh, etc , Co., 31 W. Va. 836; Society Perun v. Cleveland, 43 Ohio St. 481.

[6] Ward v. Min., etc., R. Co., 119 Ill. 287, 10 N. E. Rep. 365; McAuley v. Col., etc., R. Co., 83 Ill. 348; Reisner v. Strong, 24 Kan. 410; Asheville Div. No. 15 v. Astor, 92 N. C. 578; Wellington, etc., R. Co. v. Cashie, etc., R. Co., 114 N. C. 690.

II. Estoppel to Deny Corporate Existence.

§ 81. **General statement.**—The rule which forbids a private individual to raise the question of corporate existence in a collateral proceeding, is of the widest application and applies to all cases where the organization is a *de facto* corporation. Where, however, the objection goes to the fact of *de facto* corporate existence, as where there is no law under which the incorporation might have been effected, or where the law expressly forbids the creation of such a corporation, the rule has no application. In many cases we find that the doctrine of estoppel has been applied in such manner as to prevent one who has dealt with a corporation as such from denying that it is a corporation, in a proceeding growing out of the transaction. Where there is a *de facto* corporation, it is unnecessary to invoke the doctrine of estoppel, as the general rule of public policy forbids anyone but the state raising the question. The doctrine of estoppel is, hence, of more limited application than the general principle discussed in the preceding sections. In some cases an estoppel is applied in such manner as to prevent a party from raising the question of the legal right to become incorporated. But the authorities are conflicting, and no generally accepted rule exists.

§ 82. **The general rule.**—The rule is established that one who has contracted with a *de facto* corporation, as such, will not be permitted, after having received the benefit of his contract, to allege and prove any defect in the organization of such corporation, which affects its capacity to enforce the contract. "Where there is thus a corporation *de facto*, with no want of legislative power to its due and legal existence; where it is proceeding in the performance of corporate functions, and the public are dealing with it on the supposition that it is what it professes to be; and the questions suggested are only whether there has been exact regularity and strict compliance with the provisions of the law relating to incorporation, it is plainly a dictate alike of justice and of public policy that in controver-

sies between the *de facto* corporation and those who have entered into contractual relations with it as corporators or otherwise, such question should not be permitted to be raised."[1] Those who have engaged in organizing a corporation can not, when sued on a contract made in a corporate character, be heard to deny the fact of corporate existence.[2] This rule applies when such parties seek to escape statutory liability for its debts.[3] The grantor of a deed in which the grantee is named as a corporation, is thereafter estopped to deny the fact of incorporation.[4] The maker of a promissory note, in which the payee is named as a corporation, can not deny the fact of incorporation in an action on the note.[5] One who executes a mortgage to a corporation as such, to secure a loan of money, can not deny the corporate character to defeat an action brought to foreclose the mortgage.[6]

§ 83. **In actions against members as partners.**[7]—The weight of authority seems to support the proposition that those who deal with an association as a corporation are estopped to deny its existence as such, even for the purpose of holding its mem-

[1] Swartwout v. Michigan, etc., R. Co., 24 Mich. 389; Wadesboro, etc., Co. v. Burns, 114 N. C. 353, 19 S. E. Rep. 238; M. E. Church v. Pickett, 19 N. Y. 482; Stofflet v. Strome, 101 Mich. 197, 59 N. W. Rep. 411; Com. Bank v. Pfeiffer, 108 N. Y. 242, 15 N. E. Rep. 311; Columbia, etc., Co. v. Dixon, 46 Minn. 463; Minn., etc., Co. v. Denslow, 46 Minn. 171; B. and L. Assn. v. Chamberlain, 4 S. Dak. 271; Butchers' Bank v. MacDonald, 130 Mass. 264; Hassinger v. Ammon, 160 Pa. St. 245; Bank of Shasta v. Boyd, 99 Cal. 604; Hause v. Mannheimer, 67 Minn. 194; Perrine v. Grand Lodge, 48 Minn. 82.

[2] Fitzpatrick v. Rutter, 160 Ill. 282, 43 N. E. Rep. 392; Bon Aqua, etc., Co. v. Standard, etc., Co., 34 W. Va. 764; Scheufler v. Grand Lodge, 45 Minn. 256; Perrine v. Grand Lodge, 48 Minn. 82; Stewart, etc., Co. v. Rau, 92 Ga. 511; Farmers', etc., Co. v. Toledo, etc., R. Co., 67 Fed. Rep. 49.

[3] B. and L. Assn. v. Chamberlain, 4 S. Dak. 271, 56 N. W. Rep. 897; Slocum v. Gas-pipe Co., 10 R. I. 112; Hamilton v. R. Co., 144 Pa. St. 34; McCarthy v. Lavasche, 89 Ill. 270; Altman v. Waddle, 40 Kan. 195.

[4] Whitney v. Robinson, 53 Wis. 309, 10 N. W. Rep. 512.

[5] Stoutimore v. Clark, 70 Mo. 471; Brickley v. Edwards, 131 Ind. 3, 30 N. E. Rep. 708.

[6] Falls v. United States, etc., Co., 97 Ala. 417, 24 L. R. A. 174.

[7] See Wilgus' Cases, particularly Martin v. Fewell, 79 Mo. 401; Fay v. Noble, 7 Cush. (Mass.) 188.

bers as partners.[1] There are well-considered cases, however, which hold the contrary.[2]

Where the plaintiff was one of the organizers and a member of the first board of directors, it was held, in an action against the corporation to have it declared a co-partnership, that he was estopped to claim that the corporation had never been legally organized. If the plaintiff had been sued by the corporation on his subscription to its capital stock he "could not have questioned its corporate existence on the grounds alleged in his bill. * * * It is equally clear that if, during the time he was a member of said corporation, it had been sued as such, neither he nor any other of its members could have been heard to say that no such corporation existed. The general rule is, that one who deals with a corporation as existing *de facto*, is estopped to deny, as against it, that it has been legally organized. It is the settled rule in this state that the legal existence of a corporation *de facto* can not be questioned collaterally."[3]

§ 84. **Actions on stock subscriptions.**—In an action brought by the corporation, its receiver, or its creditors, to enforce a stock subscription, one who subscribed for the stock after the organization of the pretended corporation is estopped to deny the legality of the incorporation.[4] This is but an application of the general principle that a subscriber can not, as against creditors, set up the invalidity of a subscription to stock as to which, if valid, he was in *pari delicto*.[5] One who has been

[1]Sniders, etc., Co. v. Troy, 91 Ala. 224; Cochrane v. Arnold, 58 Pa. St. 399; Bradford v. R. Co., 142 Ind. 383, 40 N. E. Rep. 741; Black River, etc., Co. v. Holway, 85 Wis. 344, 55 N. W. Rep. 418; Phinizy v. R. Co., 62 Fed. Rep. 678; Johnston v. Gumbel (Miss.), 19 So. Rep. 100; Shields v. Land Co., 94 Tenn. 123.

[2]Friedenberg v. Lynn, etc., Church, 37 Mich. 476; and see Schloss v. Trade Co., 87 Ala. 411; De Witt v. Hastings, 69 N. Y. 518; Clarke v. Jones, 87 Ala. 474, 6 So. Rep. 362.

[3]Bushnell v. Consolidated, etc., Co., 138 Ill. 67.

[4]Hause v. Mannheimer, 67 Minn. 194; Hickling v. Wilson, 104 Ill. 54; Wheelock v. Kost, 77 Ill. 296; Hamilton v. R. Co., 144 Pa. St. 34; Craven v. Mill Co., 120 Ind. 6, 21 N. E. Rep. 981; Capps v. Hastings, etc., Co., 40 Neb. 470, 24 L. R. A. 259; Thompson v. Reno, etc., Bank, 19 Nev. 103; Chubb v. Upton, 95 U. S. 665; Wadesboro, etc., Co. v. Burns, 114 N. C. 353.

[5]Capps v. Hastings, etc., Co., 40 Neb. 470, 24 L. R. A. 259, 58 N. W.

induced by fraud to become a subscriber to the stock of a corporation is estopped from asserting the fact as a defense when he failed to repudiate the subscription until after the corporation became insolvent.[1]

§ 85. **Subscriptions in contemplation of incorporation.** When a subscription for stock is made before and in contemplation of the incorporation of a company, and there is no subsequent acquiescence such as will create an estoppel, the subscriber may insist upon a legal corporation, and defend in an action upon his contract of subscription by showing that there was no legal incorporation.[2]

"Until the statutory requirements to organize a corporation have been complied with, a subscriber to the articles of incorporation is not estopped to deny the existence of the corporation."[3]

But if such a subscriber takes an active part in the organization of the corporation or its management after organization he is thereafter estopped to deny that it was legally organized.[4]

§ 86. **Estoppel by acquiescence.**—A member of a corporation who has acquiesced in the illegal or irregular acts of the corporation is estopped to deny his liability to the corporation. Thus, if he has acted as a director, attended stockholders' meeting, paid calls, or done any other act indicating acquiescence, he can not be heard to say that the corporation is illegal, when it is sought to hold him liable for his acts as a member.[5]

Rep. 956; Rikhoff v. Brown, etc., Co., 68 Ind. 388. See Martin v. South Salem, etc , Co., 94 Va. 28. In an action by a receiver on a stock subscription the subscriber is estopped to deny the legality of the object of the corporation, where the subscription is lawful on its face. Cardwell v. Kelly, 95 Va. (1898) 570, 28 S. E. Rep. 953.

[1]Martin v. Land Co., 94 Va. 28, 26 S. E. Rep. 591. See *infra*, § 389.

[2]Schloss v. Montgomery, etc., Co., 87 Ala. 411, 6 So. Rep. 360; Columbia Elec. Co. v. Dixon, 46 Minn. 463; Doris v. Sweeny, 60 N. Y. 463; Capps v. Hastings, etc., Co., 40 Neb. 470, 58 N. W. Rep. 955, 24 L. R. A. 259; Rikhoff v. Brown, etc., Co., 68 Ind. 388; Indianapolis, etc., Co. v. Herkimer, 46 Ind. 142; Richmond Fac. Assn. v. Clarke, 61 Me. 351; Taggart v. West Md. R. Co., 24 Md. 563, Wilgus' Cases.

[3]Ind., etc., Co. v. Herkimer, 46 Ind. 143.

[4]Danbury & N. R. Co. v. Wilson, 22 Conn. 456; Phœnix W. Co. v. Badger, 67 N. Y. 294; Canfield v. Gregory, 66 Conn. 9, Wilgus' Cases.

[5]Swartwout v. Mich., etc., Co., 24

§ 87. **Estoppel limited to de facto corporations.**—The rule in many states seems to be that the doctrine of estoppel is limited to cases in which there is a *de facto* corporation in existence.[1] In a well-known case Judge Cooley said[2]: "Where there is a corporation *de facto*, with no want of legislative power to its due and legal existence, * * * it is plainly a dictate, alike of justice and public policy, that, in controversies between the *de facto* corporation and those who have entered into contract relations with it, as corporators or otherwise, such questions should not be suffered to be raised." The reasons upon which this rule rests are thus stated:[3] "The statute laws of the state expressly requiring certain prescribed acts to be done to constitute a corporation, to permit parties indirectly, or upon the principle of estoppel, virtually to create a corporation for any purpose, would be in manifest opposition to the statute and clearly against its policy, and justified upon no sound principle in the administration of justice." In another case it was said:[4] "The estoppel arises upon matter of *fact* only, and not upon matter of *law*. Hence, if there be no law which authorized the supposed corporation, or if the statute authorizing it be unconstitutional and void, the contract does not estop the party making it to dispute the existence of the corporation. But if, on the other hand, there be a law which authorized the corporation, then, whether the corporators have complied with it so as to become duly incorporated, is a question of fact, and the party making the contract is estopped to dispute the organization or the legal existence of the corporation." Where the

Mich. 389; Home, etc., Co. v. Sherwood, 72 Mo. 461; Meadow v. Gray, 30 Me. 547; Intermountain, etc., Co. v. Jack, 5 Mont. 568; Appleton, etc., Co. v. Jesser, 87 Mass. (5 Allen) 446; Central, etc., Assn. v. Ala., etc., Co., 70 Ala. 130.

[1] Heaston v. Railroad Company, 16 Ind. 275; Snyder v. Studebaker, 19 Ind. 462; Jones v. Aspen, etc., Co., 21 Colo. 263, 29 L. R. A. 143; Bandenstein v. Hoke, 101 Cal. 131; Eaton v. Walker, 76 Mich. 579, 43 N. W. Rep. 638; Maryland, etc., Works v. West End, etc., Co., 87 Md. 207, 39 L. R. A. 810.

[2] Swartwout v. Mich., etc., R. Co., 24 Mich. 390.

[3] Boyce v. Towsontown, etc., Trus., 46 Md. 373; Jones v. Aspen, etc., Co., 21 Colo. 263, 29 L. R. A. 143; Snyder v. Studebaker, 19 Ind. 462.

[4] Snyder v. Studebaker, 19 Ind. 462, Wilgus' Cases.

corporation bringing an action had not paid the state fees upon the filing of its articles of incorporation, and the statute declared that until this fee was paid the corporation should have no corporate powers, it was held that the defendant, who had dealt with the corporation as a corporation, was not estopped to assert this defense.[1]

§ 88. **The contrary doctrine—Unconstitutional statutes.**— If the doctrine of estoppel is to be limited to cases where a *de facto* corporation exists, it seems unnecessary, as all cases are covered by the rule that no one but the state can raise the question of the existence of such corporation. There are strong arguments against allowing an estoppel where there has not been sufficient done to create a *de facto* corporation, or where there is no law under which such a corporation can be organized. But there are many cases where the language used is so general that it may be understood as applying to all cases where a party deals with an organization which assumes to be a corporation.[2] There are also numerous cases[3] which hold

[1]Maryland, etc., Works v. West End, etc., Co., 87 Md. 207, 39 L. R. A. 810; Jones v. Aspen, etc., Co., 21 Colo. 263, 29 L. R. A. 143; Slocum v. Prov., etc., Co., 10 R. I. 112. A duly organized foreign corporation is a *de jure* corporation, although it has not complied with a statute which requires a foreign corporation to pay a purchase fee and making void all contracts of one not paying such fee. Rough v. Breitung (Mich. 1898), 75 N. W. Rep. 147.

[2]Close v. Cemetery, 107 U. S. 477; Winget v. Association, 128 Ill. 67, 21 N. E. Rep. 12; Building, etc., Assn. v. Chamberlain, 4 S. D. 271; Bashford, etc., Co. v. Agua, etc., Co. (Ariz.), 35 Pac. Rep. 983; Schloss v. Trade Co., 87 Ala. 411; 6 So. Rep. 360; Slocum v. Providence, etc., Co., 10 R. I. 112.

[3]Building, etc., Assn. v. Chamberlain, 4 S. D. 271, 56 N. W. Rep. 897; Wright v. Lee, 4 S. D. 237, 55 N. W. Rep. 931; Freeland v. Ins. Co., 94 Pa. St. 504; Dows v. Napier, 91 Ill. 44; Irrigation Co. v. Warner, 72 Cal. 379; St. Louis v. Shields, 62 Mo. 247; McCarthy v. Lavasche, 89 Ill. 270; Morawetz II, § 759. In Building, etc., Assn. v. Chamberlain, *supra*, the court said: "The rule in Michigan appears to be different, and when a corporation is organized under a void act of the legislature, the courts will not recognize the corporation for the purpose of enforcing a contract made by it or with it. The cases which have been decided by the supreme court of that state in which the question arose, viz: State v. How, 1 Mich. 512; Green v. Graves, 1 Doug. (Mich.) 351; Hurlbut v. Britain, 2 Doug. (Mich.) 191; Burton v. Schildbach, 45 Mich. 504; Mok v. Association, 30 Mich. 511—were cases where the corpora-

that persons who aid in organizing a corporation, subscribe for its stock and induce others to transact business with the corporation on the faith of its being legally incorporated, are estopped from alleging that the law under which the corporation is organized is unconstitutional.

tions appear to have been formed for illegal purposes, namely, to violate laws against unauthorized banking, as well as without constitutional legislative authority. But that court seems to have receded somewhat from this position in the later case of Manufacturing Co. v. Runnells, 55 Mich. 130, 20 N. W. Rep. 823," Wilgus' Cases.

CHAPTER 4.

THE CORPORATION AND THE STATE[1]—THE CHARTER.

§ 89. The control of the state.
90. Visitorial power.
91. Corporations of a *quasi*-public character.
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118. Telegraph companies.
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§ 89. **The control of the state.**—Every corporation is subject to the control of the state, the power by which it is created. This control must, however, be exercised subject to the restrictive provisions contained in the state and national constitutions. The relations between the state and a corporation may be contractual, and are then governed by the same general principles of law which govern contracts between individuals.[2]

[1] See Wilgus' Cases, The Corporation and the State.

[2] A corporation is a person within the meaning of the 14th amendment to the constitution of the United States. Hammond, etc., Co. v. Best,

§ 90. **Visitorial power.**—All corporations are subject to the visitorial power of the state; *i. e.*, to the control and inspection of tribunals created by the law of the land. Civil corporations are visited by the government itself through the medium of the courts of justice; but the internal affairs of ecclesiastical and eleemosynary corporations are, in general, inspected and controlled by a private visitor.[1] Civil corporations being created for public use and advantage, properly fall under the superintendency of the sovereign power whose duty it is to take care of the public interest; but corporations whose object is the distribution of a private benefaction may well find jealous guardians in the zeal or vanity of the founder, his heirs or appointees.[2] The present power of control over corporations is founded more on grounds of public policy than on any theory of succession to the rights of a prehistoric founder. As a general rule the state has the same control, in this respect, over corporations that it has over individuals.[3]

§ 91. **Corporations of a quasi-public character.**—The state exercises extensive control over private corporations which have a public character, such as railways, water, gas, telegraph and telephone corporations. Certain corporations, like banks, are, to a certain extent, agencies of government, while the control over others is based upon the extraordinary powers and franchises which have been granted to them. This is particularly true of common carriers and corporations which exercise the power of eminent domain. Thus the rates and contracts of these corporations are subject to the control of the

91 Me. 431, 42 L. R. A. 529; see § 68, *supra*; Santa Clara Co. v. Southern, etc., R. Co., 118 U. S. Rep. 394; Memphis, etc., R. Co. v. Beckwith, 129 U. S. Rep. 26.

[1] Phillips v. Bury, 2 T. R. 346. See Wilgus' Cases, Visitation.

[2] Angell & Ames Priv. Corps., § 684, Kyd Corp., 174, 1 Black. Com., p. 280, 2 Kent Com., p. 300; Burney's Case, 2 Bland. Ch. 141; Wisconsin, etc., Co. v. Milwaukee Co., 95 Wis. 153, 36 L. R. A. 55.

[3] Bank v. Hamilton, 21 Ill. 53. A court will not exercise visitorial power over a foreign corporation. See Clark v. Mutual, etc., Co. (D. C.), 43 L. R. A. 391. The old law of visitation does not apply to modern business corporations. The so-called visitorial power over them is in the courts. See State v. Georgia, etc., Society, 38 Ga. 608, 95 Am. Dec. 408, Wilgus' Cases.

state, which generally acts through a board of visitors, such as railway commissioners or interstate commerce commissions.[1] The power of these bodies is very extensive, and in some cases, where they have discretionary power, no appeal lies from their decision,[2] unless there has been fraud, or its exercise results in practical confiscation of property.[3] Water and gas companies are subject to extensive control. Thus a water company may be compelled to supply water to all impartially at reasonable rates, and will be enjoined from cutting off the water supply from any one without good cause.[4] The rates may be fixed by commissioners. The same control is exercised over gas companies.[5] They must not act arbitrarily.[6] Thus, where there is a chance that the charges are erroneous, notwithstanding the reading of the meter, the company will be enjoined from cutting off the supply till the matter can be determined in a court of law.[7] Such a corporation must furnish gas to all who comply with reasonable regulations.[8] The company can not refuse to furnish gas to the occupant of certain premises because he has not paid an account incurred for gas while occupying other premises.[9] Telegraph and telephone companies are subject to the same control as other common

[1] State v. Cincinnati, etc., R. Co., 47 Ohio St. 130, 23 N. E. Rep. 928; Minneapolis, etc., R. Co. v. Railroad Commissioners, 44 Minn. 336, 46 N.W. Rep. 559; State v. Mo. Pac. R. Co., 29 Neb. 550, 45 N. W. Rep. 785; Central, etc., R. Co. v. State (Ga.), 42 L. R. A. 518.

[2] See Minneapolis, etc., R. Co. v. Railroad Commissioners, 44 Minn. 336.

[3] San Diego, etc., Co. v. San Diego, 118 Cal. 556, 38 L. R. A. 460, and cases cited. But see Smyth v. Ames, 169 U. S. 466.

[4] American, etc., Co. v. State, 46 Neb. 194, 30 L. R. A. 447; State v. Butte City, etc., Co., 18 Mont. 199, 32 L. R. A. 697. See notes in 15 L. R. A. 321 and 29 L. R. A. 376.

[5] Water-works v. Schottler, 110 U. S. 347, Wilgus' Cases.

[6] See generally Ernst v. New Orleans, etc., Co., 39 La. Ann. 550, 2 So. Rep. 415; McCrary v. Beaudry, 67 Cal. 120; Silkman v. Yonkers Water Comrs., 152 N. Y. 327, 37 L. R. A. 827. Water rates not a tax. Wagner v. Rock Island, 146 Ill. 139, 21 L. R. A. 519.

[7] Sickles v. Manhattan, etc., Co., 66 How. (N. Y.) 305.

[8] Coy v. Indianapolis, etc., Co., 146 Ind. 655, 36 L. R. A. 535.

That a person is already supplied with gas by another company is no justification. Portland, etc., Co. v. State, 135 Ind. 54, 21 L. R. A. 639.

[9] Lloyd v. Washington, etc., Co., 1 Mackey (D. C.) 331.

carriers.[1] But every corporation is not necessarily obliged to deal with the whole community. Thus a board of trade may decide among what outside persons its telegraphic reports shall be distributed.[2] But a corporation organized for the purpose of transmitting stock quotations by telegraph is of a quasi-public character, and must serve all who are willing to pay for the service.[3]

§ 92. **Reports.**—All private corporations may be required to make periodical reports of their capital, business and general condition to a state board or official. But a failure to do so does not itself work a forfeiture of the charter,[4] although it may render the directors personally liable for the debts of the corporation,[5] and under some circumstances may be a good ground of forfeiture.[6] But usually if *quo warranto* is brought for failure to file reports, the state will accept a tender of the reports.[7]

§ 93. **Consequences of illegal or ultra vires acts.**—In order that the state may retain control over corporations, it is necessary that it should have the power to restrain or punish unauthorized acts. It may do this by *scire-facias* or *quo warranto.* The exercise by a private corporation of franchises or privileges not conferred by law may result in the forfeiture of the charter [8] or in merely ousting the corporation from the exercise of the powers illegally assumed.[9] If the corporation violates its charter or fails in the performance of its corporate duties in material and important particulars, there will generally be a judgment of ouster.[10] But according to modern authorities this result does not necessarily follow when the corporation has entered into *ultra vires* contracts which are not

[1] Central Union, etc., Co. v. Bradbury, 106 Ind. 1; State v. Nebraska, etc., Co., 17 Neb. 126, 52 Am. Rep. 404; American, etc., Co. v. Connecticut, etc., Co., 19 Conn. 352, 44 Am. Rep. 237. See generally notes in 24 Am. L. Reg. N. S. 573, 59 Am. Rep. 172, 175, 41 Am. Rep. 211, 243, 38 Am. Rep. 589.

[2] Marine, etc., Exchange v. Western Union, etc., Co., 22 Fed. Rep. 23, and note to 17 Fed. Rep. 23; Metropolitan, etc., Exchange v. Chicago Board of Trade, 15 Fed. Rep. 817.

[3] Friedman v. Gold, etc., Co., 32 Hun (N. Y.) 1.

[4] State v. Brownton, etc., R. Co., 120 Ind. 337, 22 N. E. Rep. 316.

[5] Post Express, etc., Co. v. Coursey (N. Y.), 10 N. Y. Supp. 497.

[6] Attorney-General v. Petersburg R. Co , 6 Ired. (N. C.) 456.

[7] State v. Barron, 57 N. H. 498.

[8] People v. Pullman, etc., Co., 175 Ill. 126; Hartnett v. Plumbers', etc., Assn. (Mass.), 47 N. E. Rep 1002, 38 L. R. A. 194; State v. Pennsylvania, etc., Co., 23 Ohio St. 121.

[9] People v. Building Assn., 35 Ohio St. 258.

[10] People v. N. R., etc., Co., 121 N. Y. 582; People v. Chicago, etc., Exchange, 170 Ill. 556, 39 L. R. A. 373; Capital City, etc., Co. v. State, 105 Ala. 406, 29 L. R. A. 743.

prohibited because contrary to morals or express statute. *Ultra vires* acts are not necessarily a misuse of franchises to such an extent as will warrant their forfeiture. A certain measure of discretion is exercised, and it is safe to assume that so severe a penalty will follow only when the act is of such a nature as to affect the public interests.[1] As a result a corporation may do many things which are not authorized by its charter, and the state will not interfere so long as the stockholders or other private persons only are affected thereby. Of course, where the statute provides that certain acts shall be punished by forfeiture the courts have no discretion.[2] The proper proceeding is by *quo warranto* on the motion of the attorney-general or on the relation of some citizen.[3]

A court of equity does not sit to administer punishment or enforce forfeitures for violations of law; its jurisdiction is limited to the protection of civil rights, and the cases in which full and adequate relief can not be had at law. An ice company imported two cargoes of tea, and the attorney-general filed an information in equity to restrain the company from longer carrying on the ice business. The court said:[4] "The company is a private trading corporation. It is not in any sense a trustee for public purposes. This is not a suit by a stockholder or a creditor. The acts complained of are not shown to have injured or endangered any rights of the public or any individual or other corporation, and can not upon any

[1] State v. Minnesota, etc., Co., 40 Minn. 213; Thompson Priv. Corp., § 6034; article by Jesse W. Lilienthal, in 11 Harv. Law Rev. 387, on Non-Public Corporations and *Ultra Vires*. In People v. N. R. Ref. Co., 121 N. Y. 582, the court said that to justify forfeiture of corporate existence "the state must show, on the part of the corporation accused, some sin against the law of its being which has produced or tends to produce injury to the public. The transgression must not be merely formal or incidental, but material or serious, or such as to harm or menace the public welfare; for the state does not concern itself with the quarrels of private litigants. It furnishes for them sufficient courts and remedies, but intervenes as a party only when some public interest requires its action."

[2] State v. Pennsylvania, etc., Co., 23 Ohio St. 121; State v. Oberlin, etc., Assn., 35 Ohio St. 258.

[3] Attorney-General v. Utica, etc., Co., 2 John. Ch. 371; People v. Utica, etc., Co., 15 John. 358, Wilgus' Cases.

[4] Attorney-General v. Tudor, etc., Co., 104 Mass. 239, Wilgus' Cases.

legal construction be held to constitute a nuisance. * * * No case is therefore made upon which, according to the principles of equity jurisprudence and the practice of this court, an injunction should be issued upon an information in chancery." But when a *quasi*-public corporation is doing and contemplating acts which are *ultra vires* and illegal, the necessary effects of which are not only to impair the rights of the public, but also to create a nuisance, an injunction will issue. The principle here is that the court has jurisdiction to restrain and prevent nuisances, and where the nuisance is a public one, information by the attorney-general is the appropriate remedy.[1] Grounds of forfeiture must be taken advantage of through the law courts. The state does not waive the forfeiture by recognizing the corporation as such after a cause for forfeiture exists. Notwithstanding an existing ground of forfeiture, the corporation may continue to exercise its franchises until judgment of ouster is pronounced.[2]

§ 94. **Forfeiture distinguished from repeal.**—The repeal of a charter by the legislature under a reserve power, must be distinguished from a forfeiture. The legislature exercises the power of repeal in accordance with the conditions of the contract, while a court declares a forfeiture for non-user or misuser of corporate franchises or powers, independent of any reserved right.[3] A corporation is not dissolved by an act of non-user or misuser, which is a cause of forfeiture of its franchise. The franchise exists until the forfeiture is declared in a judicial proceeding by the state against the corporation for that purpose, unless a contrary legislative intent is clearly manifested.[4] The statute required a turnpike company to

[1] Attorney-General v. Aqueduct Corporation, 133 Mass. 361.

[2] People v. Bank, 24 Wend. (N. Y.) 431.

[3] Erie, etc., R. Co. v. Casey, 26 Pa. St. 287; Detroit v. Plank Road Co., 43 Mich. 140.

[4] State v. Atchison, etc., R. Co., 24 Neb. 143, 8 Am. St. Rep. 179; Atchison, etc., R. Co. v. Nave, 38 Kan. 744, 5 Am. St. Rep. 803. In State v. Spartanburg, etc., R. Co. (S. C.), 28 S. E. Rep. 145, it was held that the failure to complete a railroad under the provisions of the company's charter,—to the effect that the powers, rights, privileges, and immunities granted thereby should cease, determine, and be void

make an annual report to the legislature "under forfeiture of the privileges of the act in future." The court said: "The meaning of this is that the forfeiture shall be proved in the regular legal manner; upon the institution and prosecution of proceedings in the established course, such neglect of this duty shall be cause of forfeiture."[1]

§ 95. **The charter.**—The charter of a corporation is the act or acts of the legislature by which the corporation is created and its powers and franchises granted. Under general corporation laws the articles of incorporation, read in connection with the general laws of the state, constitute the charter.[2]

§ 96. **The charter as a contract.**—Each corporate charter contains at least one contract, the franchise of being a corporation. This privilege "is a distinct, independent, essential franchise," complete within itself, having no necessary connection with other distinct franchises, which are the subjects of legislative grant and which may or may not be given to corporations once created, as well as to natural persons, as to the legislature may seem advisable.[3]

The franchise of acting as a private corporation is a contract between the state and the incorporators, which can not be impaired by the subsequent acts of the state without violating the constitutional provision which forbids the states to pass laws impairing the obligation of a contract.[4] "It is now too late to contend that any contract which a state actually enters into, when granting a charter to a private corporation, is not within the protection of the clause in the constitution of the United States that prohibits states from passing laws impairing

unless the company shall complete the road within three years,—is merely a cause of forfeiture, and not an express limitation of the existence of the corporation, and does not *ipso facto* dissolve the corporation. But see The Brooklyn, etc., Co. v. City of Brooklyn, 78 N. Y. 524, Wilgus' Cases.

[1] State v. Turnpike, 15 N. H. 162.

[2] Lincoln, etc., Co. v. Sheldon, 44 Neb. 279, 62 N. W. Rep. 480; North, etc., Co. v. Utah, etc., Co. (Utah), 52 Pac. Rep. 168, 40 L. R. A. 851; Louisville Water Co. v. Clark, 143 U. S. 1; People v. Chicago, etc., Co., 130 Ill. 268.

[3] Southern, etc., R. Co. v. Orton, 32 Fed. Rep. 457, Wilgus' Cases.

[4] Const. U. S., Art. 1, § 10. Dartmouth College v. Woodward, 4 Wheat. 518; Cary, etc., v. Bliss, 151 Mass. 364, 25 N. E. Rep. 92; Downing v. Board, 129 Ind. 443, 28 N. E. Rep. 123, 614; Zimmers v. State, 30 Ark. 677. The rule applies to private corporations only.

the obligation of contracts. The doctrines of Dartmouth College v. Woodward, announced by this court more than sixty years ago, have become so imbedded in the jurisprudence of the United States as to make them to all intents and purposes a part of the constitution itself. In this connection, however, it is to be kept in mind that it is not the charter that is protected, but only any contract which the charter may contain. If there is no contract there is nothing in the grant on which the constitution can act; consequently, the first inquiry in this class of cases always is: whether a contract has in fact been entered into, and if so, what its obligations are."[1]

§ 97. **The Dartmouth College case.**—Of this famous case[2] Mr. Justice Miller said:[3] "It may well be doubted whether any decision ever delivered by any court has had such a pervading operation and influence in controlling legislation as this. It is founded upon the clause of the constitution which declares that no state shall make any law impairing the obligation of contracts. Dartmouth College existed as a corporation under a charter granted by the British crown to its trustees in New Hampshire in the year 1769. This charter conferred upon them the entire governing power of the college, and, among other powers, that of filling up all vacancies occurring in their own body, and of removing and appointing tutors. It also declared that the number of trustees should forever consist of twelve, and no more.

"After the revolution the legislature of New Hampshire passed a law to amend the charter and to improve and enlarge the corporation. It increased the number of trustees to twenty-one, gave the appointment of the additional members to the

[1] Chief Justice Waite in Stone v. Mississippi, 101 U. S. 814.

[2] 4 Wheat. (U. S.) 518.

[3] For an "inside" history of the case, see Shirley's "The Dartmouth College Case and the Supreme Court of the United States." For criticisms, see Ashuelot R. Co. v. Elliot, 58 N. H. 451, and an article by Seymour D. Thompson, 26 Am. Law Rev. 169. See criticism by Chief Justice Bartley, in Toledo Bank v. Bond, 1 Ohio St. 626, *et seq.* (1853). The manifold applications of the doctrines of the case and their limitations are best set forth by Mr. Justice Brown in Pearsall v. Great Northern R. Co., 161 U. S. 646, Wilgus' Cases. I have given the statement of this famous case in the authoritative language of Mr. Justice Miller, used in his Lectures on the Constitution, page 392.

executive of the state, and created a board of overseers, to consist of twenty-five persons, of whom twenty-one were also to be appointed by the executive of New Hampshire. These overseers had power to inspect and control the most important acts of the trustees. The supreme court, reversing the decision of the superior court of New Hampshire, held that the original charter constituted a contract between the crown, in whom the power was then vested, and the trustees of the college, which was impaired by the act of the legislature above referred to. The opinion, to which there was but one dissent, establishes the doctrine that the act of a government, whether it be by a charter of the legislature or of the crown, which creates a corporation, is a contract between the state and the corporation and that all the essential franchises, powers and benefits conferred upon the corporation by the charter become, when accepted by it, contracts within the meaning of the clause of the constitution referred to. The opinion has been of late years much criticised, as including with the class of contracts whose foundation is within the legislative action of the states, many which were not properly intended to be so included by the framers of the constitution, and it is undoubtedly true that the supreme court itself has been compelled of late years to insist in this class of cases upon the existence of an actual contract by the state with the corporation when relief is sought against subsequent legislation."

§ 98. **Contracts contained in charter.**[1]—The contracts which are ordinarily found in the charter of a private corporation fall into three classes:

(1.) Those between the state and the incorporators,[2] such

[1] See especially, opinion of Story, in Dartmouth College v. Woodward, Wilgus' Cases,

[2] The Delaware Railroad Tax, 18 Wall. 206; Bank of Pa. v. Comw., 19 Pa. St. 144. In Thorpe v. Rutland & Burlington R. Co., 27 Vt. 141 (1885), Redfield, C. J., said: "It is admitted that the essential franchise of a private corporation is recognized by the best authorities as private property, and can not be taken without compensation, even for public use. * * * All the cases agree that the indispensable franchises of a corporation can not be destroyed or essentially modified. This is the very point upon which the leading case of Dartmouth College v. Woodward was decided, and which every well considered case in this country maintains."

as the franchise of acting as a corporation, of exemption from taxation,[1] or that the charter shall not be subject to amendment or repeal without the consent of the corporation.[2]

(2.) Contracts between the corporation and the stockholders. When one becomes a member of a corporation, it is upon certain terms and conditions and for certain specified purposes. He subjects his interests to the control of proper authorities to accomplish the object of the organization, but he does not agree that the purpose shall be changed in its character at the will of the directors, or a majority of the stockholders even. The contract can not be changed without the consent of both parties.[3] Hence there arises a contract which the legislature can neither impair, nor authorize a majority of the members to impair. Thus, where the act of incorporation provides for the election of directors by majority vote, it is not within the power of the legislature to change the method of voting so as in effect to place the control in the hands of a minority,[4] or provide for cumulative voting.[5] So a law authorizing consolidation with another corporation and the transfer of the property to the consolidated company is invalid.[6] The contract between the corporation and its stockholders is violated by a statute which authorizes a majority of the stockholders to engage in a business not authorized by the charter.[7]

(3.) Contracts between the corporation and persons dealing with the corporation; such as statements in the charter or law, that the capital stock shall be a certain amount, or that the stockholders of an insolvent corporation shall be liable for an amount in excess of the face value of their stock.[8]

[1] New Jersey v. Wilson, 7 Cranch 164.

[2] Louisville Gas Co. v. Citizens', etc., Co., 115 U. S. 683.

[3] Clearwater v. Meredith, 1 Wall. 25.

[4] Hays v. Commw., 82 Pa. St. 518.

[5] State v. Greer, 78 Mo. 188; Hays v. Commw., 82 Pa. St. 518; Orr v. Bracken Co., 81 Ky. 593. But see Cross v. Railroad Co., 35 W. Va. 172.

[6] Lauman v. R. Co., 30 Pa. St. 46.

[7] Zabriskie v. R. Co., 18 N. J. Eq. 178.

[8] Hawthorn v. Calef, 2 Wall. 10; McDonnell v. Alabama, etc., Co., 85 Ala. 401; Norris v. Wrenschall, 34 Md. 492; Sinking Fund Cases, 99 U. S. 700; Conant v. VanSchaick, 24 Barb. 89. Where the liability is placed upon an officer as a penalty for failing to comply with the statutory requirement, all rights of the creditor are lost by a repeal of the statute. There is no such thing as a vested interest in an unenforced penalty. Gregory v. Ger-

§ 99. **Reservation of right to repeal or amend charter.**—Since the decision of the Dartmouth College case the states generally reserve the right to repeal or amend corporate charters without the consent of the corporation. The reservation may be in the particular charter, but is now commonly contained in a constitutional provision or a general law.[1] Such general reservations apply to all charters granted or enabling acts passed subsequent to their adoption unless expressly exempted therefrom.[2] A charter accepted while a law containing a reservation of power to repeal or amend corporate charters is in existence is subject to such conditions, although the act creating the corporation contains no reference to the reservation.[3] A reservation of power to amend or repeal a charter contained in a general incorporation law, has been held not to affect specific legislation applicable only to a single city or corporation.[4]

A corporation formed by consolidation after the adoption of a constitution reserving the right to amend, alter or repeal charters, is subject to that provision, although the original corporation was not.[5]

§ 100. **Exercise of the reserve power—Illustrations.**—When the power to amend or repeal the charter is thus reserved, it is to be exercised by the legislature, and according to the weight

man Bank, 3 Colo. 336; Breitung v. Lindauer, 37 Mich. 217; Union Iron Co. v. Pierce, 4 Biss. 327; Cooley Const. Lim. (5th ed.), 444, 474; Wait Insolv. Corps., § 600.

[1] Greenwood v. Freight Co., 105 U. S. 13; Tomlinson v. Jessup, 15 Wall. (U. S.) 454; Iron City Bank, Pittsburg, 37 Pa. St. 341. See note on repeal or modification of charters and franchises, 21 Am. St. Rep. 148; also on reservation of power to alter charters, 7 Am. St. Rep. 721.

[2] Close v. Greenwood, etc., Co., 107 U. S. 466; Miller v. New York, 15 Wall. 478; The Monongahela, etc., Co. v. Coon, 6 Pa. 379; Pa. R. Co. v. Duncan, 111 Pa. St. 352. "In these instances the power of revocation was reserved in the organic law, and therefore necessarily inherent in every other; but a legislative declaration that all future charters shall be subject to modification or appeal will enter into and qualify every subsequent act of incorporation which does not clearly indicate a different design." Hare Am. Const. Law II, p. 654.

[3] Jackson v. Walsh, 75 Md. 304, 23 Atl. Rep. 778.

[4] Central, etc., Co. v. Citizens,' etc., R. Co., 80 Fed. Rep. 218.

[5] Smith v. Lake Shore, etc., R. Co. 114 Mich. 460, 72 N.W. Rep. 328; Pearsall v. Great Northern Ry., 161 U. S. 646. See Lake Shore, etc., R. Co. v. Smith, 173 U. S. 684, reversing the holding of the state court.

of authority its action can not be controlled by the courts.[1] If the reservation is of the right to repeal if certain conditions are not complied with, there may be a repeal without a previous judicial determination of failure to comply.[2] In some jurisdictions it is held that although the legislature may exercise the power before a judicial investigation, its acts are subject to review by the courts.[3] Alterations must be reasonable, made in good faith, and consistent with the scope and object of the act of incorporation.[4] Where the reservation is of power to repeal

[1] Spring Valley W. W. v. Schottler, 110 U. S. 347; Greenwood v. Freight Co., 105 U. S. 13.

[2] Miners' Bank v. U. S., 1 Greene 553 (Ia.), s. c. 43 Am. Dec. 115; Oakland R. Co. v. Oakland R. Co., 45 Cal. 365; N. Y., etc., R. Co. v. Boston, etc., R. Co., 36 Conn. 196; *contra*, Flint, etc., R. Co. v. Woodhull, 25 Mich. 99; State v. Noyes, 47 Me. 189. In Myrick v. Brawley, 33 Minn. 377, the court said: "The insertion in legislative grants, like the one in question, of express provisions for forfeiture in case of non-user or misuser, is not uncommon, and it can hardly be questioned that it is competent for the legislature, which is the law-making power, as well as one of the contracting parties, to provide in the grant a mode of enforcing the forfeiture, either by repeal of the act making the grant or otherwise, and there can be as little doubt that the forfeiture will be effectually enforced by resort to the stipulated mode, provided the event on which it is to be resorted to has arisen. Where the right reserved to recall the grant depends on the happening of a contingent event, the existence of the fact at the time of the recall must, of course, be a matter for judicial investigation. Whether the re-entry by a private grantor perfects a forfeiture must depend on the fact of condition broken, and that must be ascertained by the judiciary; but in no case, where the forfeiture may be enforced by act of the grantor, need he secure, before he enforces it, a judicial determination, that the fact upon which the right to forfeiture depends exists. The courts will decide upon the effect of his act subsequently. But neither does the legislature, when it exercises a reserved right to repeal, nor the private grantor, when he exercises a reserved right of re-entry, perform any judicial function. The act of neither assumes to determine finally the rights of the parties as effected by the act to enforce the forfeiture, That is necessarily and inherently a judicial question." Erie, etc., R. Co. v. Casey, 26 Pa. St. 287; Crease v. Babcock, 23 Pick. 334; McLaren v. Pennington, 1 Paige 102; Read v. Frankfort Bank, 23 Me. 318. As to whether a judicial act declaring a forfeiture is not necessary for the non-performance of a condition in a grant on franchise, see note to Atchison, etc., Co. v. Nave, 38 Kan. 747, 5 Am. St. Rep. 804. Mere non-action does not destroy a franchise, although it may justify a forfeiture by judicial proceedings. Higgins v. Downward, 8 Houst. 227, 40 Am. St. Rep. 141, Wilgus' Cases.

[3] Erie, etc., Co. v. Casey, 26 Pa. St. 287.

[4] The Sinking Fund Cases, 99 U. S.

or amend "at the pleasure of the legislature," the motives of the legislature are immaterial.[1] A statute requiring railroads to issue mileage books good for two years, and fixing the minimum price thereof, is not within the reserve power to alter, amend or repeal the charter of a railroad corporation.[2] A statute making the validity of a lease by a railroad company, whose charter vests the power of making such a lease in the stockholders, dependent upon its acceptance by the board of directors, is an amendment to the charter.[3] Under this reserve power the legislature may require a railroad company to change its grade and make new structures at crossings.[4] So such companies may be compelled to unite in and extend their tracks to a union passenger station, and to discontinue the use of their former station.[5] A corporation may be required to establish a sinking fund.[6] The legislature has power, according to some authorities, under the reserve power to alter or amend, to authorize cumulative voting at stockholders' meeting in corporations previously formed.[7]

§ 101. **Effect of dissolution of corporation.**—The dissolution of a corporation does not impair the obligation of contracts between the company and third persons. In a well known case,[8] Mr. Justice Story said: "The dissolution of the corporation under the acts * * * can not in any just sense be considered within the clause of the constitution of the United States on this subject an impairing of the obligation of the contracts of the company by those states any more than the death of a private person can be said to impair the obligation of his contracts. The obligation of those contracts survives, and the

700; Shields v. Ohio, 95 U. S. 319; Flint, etc., R. Co. v. Woodhull, 25 Mich. 99.

[1] Greenwood v. Freight Co., 105 U. S. 13.

[2] Lake Shore, etc., R. Co. v. Smith, 173 U. S. 684, overruling Smith v. Lake Shore, etc., R. Co., 114 Mich. 460, 72 N. W. Rep. 328.

[3] Opinion of Judges (N. C.), 28 S. E. Rep. 18.

[4] Comw. v. Eastern, etc., R. Co., 103 Mass. 254; Albany, etc., R. Co. v. Brownell, 24 N. Y. 345.

[5] Mayor v. Norwich, etc., R. Co., 109 Mass. 103.

[6] Union, etc., Co. v. U. S., 99 U. S. 700.

[7] Cross v. R. Co., 35 W. Va. 172. *Contra*, Orr v. Bracken Co., 81 Ky. 593. *Supra*, § 98.

[8] Mumma v. Potomac Co., 8 Pet. (U. S.) 281. See People v. O'Brien, 111 N. Y. 1, 52 N. Y. Sup. Ct. 519.

creditors may enforce their claims against any property belonging to the corporation which has not passed into the hands of *bona fide* purchasers, but is still held in trust for the company, or for the stockholders thereof at the time of its dissolution, in any mode permitted by the local laws." Upon an absolute repeal of a corporate charter by the legislature acting within its constitutional authority the corporation ceases to exist, and no judgment can thereafter be rendered against it.[1] If the legislature has not provided some method for protecting the rights of creditors and stockholders in case of a dissolution of a corporation, the court will protect them by such means as are within its power.[2]

§ 102. **Vested rights—Reservation of power.**—The state can not, by virtue of power reserved to repeal, amend or alter corporate charters, destroy rights which have become vested in the corporation. The power thus reserved can be exercised only for the purpose of controlling the corporation and carrying out the purposes of the original grant. "Sheer oppression and wrong can not be inflicted under the guise of amendment or alteration. Beyond the sphere of reserved powers, the vested rights and property of corporations, in such cases, are surrounded by the same sanctions and are as inviolable as in other cases."[3]

Upon the repeal of the corporate charter the life of the corporation is ended, but the property of the corporation, including street franchises, mortgages and valid contracts, survive.[4]

[1] Thornton v. Marginal R. Co., 123 Mass. 32; Marion, etc., Co. v. Ferry, 74 Fed. Rep. 426; Nelson v. Hubbard, 96 Ala. 238, 17 L. R. A. 375; Combes v. Mil., etc., R. Co., 89 Wis. 297, 27 L. R. A. 369.

[2] Greenwood v. Freight Co., 105 U. S. 13. See § 606, *infra*.

[3] Shields v. Ohio, 95 U. S. 319; Close v. Glenwood, etc., 107 U. S. 466.

[4] People v. O'Brien, 111 N. Y. 1. In Fletcher v. Peck, 6 Cranch (U. S.) 87, Chief Justice Marshall said: "If an act be done under a law, a succeeding legislature can not undo it. The past can not be recalled by the most absolute power. Conveyances have been made; these conveyances have vested legal estates, and if those estates can be seized by the sovereign authority, still that they were originally vested is a fact and can not cease to be a fact. When, then, a law is in the nature of a contract, when absolute rights have vested under that contract, a repeal of the law can not divest those rights."

A corporation authorized to construct a dam across a river may afterward be required to construct and maintain a fishway in the dam. But after this is done and the corporation, in consideration of a grant of enlarged powers, has paid certain damages caused by the construction of the dam with a fishway which the legislature knew to be insufficient, the legislature can not legally require the corporation to construct a new fishway at great cost.[1]

Where a plank road company had power to maintain a road within the city limits and to charge toll, an act which requires all plank road companies "to discontinue and remove said toll gates beyond the limits of the city" was held invalid.[2] A bare, unexecuted power to consolidate with other corporations given to a railroad company by its charter, is not, while unexecuted, a vested right protected from control or revocation by the legislature.[3]

§ 103. **Acceptance of amendment.**—Although the state reserves the right to amend the charter of a corporation, it can no more compel the acceptance of such an amendment than of an original charter. The corporation has the option of accepting the amendment or going out of existence.[4] If the corporation acts under the amendment, it will be presumed to have accepted the same.[5] The mere collecting of tolls in conformity with reduced rates fixed by a statute does not show an assent by a turnpike company to the exercise by the legislature of the power to amend its charter.[6]

§ 104. **Amendment must not create a new charter.**—The power to amend does not include the power to so far alter a charter as to change the nature and purpose of the corporation. Under a charter which authorized the amendment of the arti-

[1] Comw. v. Essex Co., 13 Gray (Mass.) 239.

[2] Detroit v. Detroit, etc., Co., 43 Mich. 140.

[3] Pearsall v. Great Northern, etc., R. Co., 161 U. S. 646.

[4] Com. v. Cullen, 13 Pa. St. 133; Yeaton v. Bank, 21 Grat. (Va.) 593; Ellis v. Marshall, 2 Mass. 279, Wilgus' Cases.

[5] Miller v. Insurance Co., 92 Tenn. 167; Demarest v. Flack, 128 N. Y. 205.

[6] Covington, etc., Co. v. Sandford, 164 U. S. 578.

cles of incorporation, provided the original purpose of the corporation should not be substantially changed, it was held that a corporation organized for the business of manufacturing gas and electricity, and furnishing gas for light, heat, power and other purposes, could not so change its articles by amendment as to become empowered to own and operate a street railway, to be operated by electricity or other motive power over a certain route, with power to extend its line beyond the city limits.[1] The rule is that the state may repeal or supersede, alter or modify a charter, but it can not take away the charter, propose a new one and oblige the stockholders to accept it. Power to alter or modify, does not imply power to substitute a thing entirely different.[2]

§ 105. **Offer of amendment.**[3]—When an amendment to a corporate charter can not lawfully be imposed by the legislature, because the power is not reserved, but is offered to a corporation for its acceptance, it may be accepted or rejected by the stockholders without having any effect upon their right to proceed under the existing charter. If the proposed amendment is fundamental and changes the original plan of the corporation, it can only be accepted by the unanimous vote of the stockholders.[4] If, however, it is merely auxiliary and in-

[1] State v. Taylor, 55 Ohio St. 61, 44 N. E. Rep. 513.

[2] Zabriskie v. Hackensack, etc., R. Co., 18 N. J. Eq. 179. Where it appeared that after the defendant subscribed for stock, the name of the corporation, the amount of the capital stock, and the extent of railway was increased by the amendment of the charter, the court said: "The right to alter was reserved in the charter and the subscription must be taken to have been made subject to having such additional powers conferred as the legislature might deem essential and expedient. The new powers conferred are identical in kind with those originally given. They are enlarged merely, the general objects and purposes of the corporation remaining still the same. It may be admitted that, under this reserve power to alter and repeal, the legislature would have no right to change the fundamental character of the corporation and convert it into a different legal being." Buffalo, etc., R. Co. v. Dudley, 14 N. Y. 336; Durfee v. Old Colony, etc., R. Co., 5 Allen (Mass.) 230; Ashuelot, etc., R. Co. v. Elliot, 52 N. H. 387, 58 N. H. 451.

[3] See Wilgus' Cases, Power of Majority.

[4] Winter v. Muscogee, etc., Co., 11 Ga. 438; Ellis v. Marshall, 2 Mass. 279. See note to Comm. v. Cullen, 53 Am. Dec. 461.

cidental and in aid of the original design, it may be accepted by a majority of the stockholders.[1]

§ 106. **Illegal amendment—Remedies.**—When a fundamental amendment to the charter has been wrongfully accepted by a corporation without the consent of all the stockholders, a dissenting stockholder who acquired his interest before the amendment was made[2] may obtain a perpetual injunction restraining action under the amendment[3] or may refuse to pay his subscription.[4] There are a few cases which hold that a dissenting stockholder may restrain action under the amendment only until the corporation offers to purchase his interest,[5] but these decisions have been criticised and are not consistent with the general current of authorities.[6] In all cases equity will aid only such stockholders as have not acquiesced in the action of the majority and have acted promptly.[7]

§ 107. **Implied contracts—Grant of exclusive franchise.**—In the absence of a constitutional prohibition the state may grant an exclusive franchise to a corporation. The charter

[1] Durfee v. Old Colony R. Co., 5 Allen (Miss.) 230; Zabriskie v. Hackensack, etc., Co., 18 N. J. Eq. 178; Black v. Canal Co., 24 N. J. Eq. 455; Woodford v. Union Bank, 3 Cold. (Tenn.) 488; Ill., etc., R. Co. v. Zimmer, 20 Ill. 658; Supervisors v. M., etc., Co., 21 Ill. 338. As to the powers of a majority, see § 486, *infra*.

[2] McClure v. People's, etc., Co., 90 Pa. St. 269.

[3] Mowrey v. Ind., etc., R. Co., 4 Biss. (C. C.) 78.

[4] Clearwater v. Meredith, 1 Wall. 25; Greenbrier v. Rodes (W. Va.), 17 S. E. Rep. 305; Youngblood v. Ga., etc., Co., 83 Ga. 797, 10 S. E. Rep. 124; Champion v. Memphis, etc., R. Co., 35 Miss. 692; Stevens v. R. & B. R. Co., 29 Vt. 545. In Mercantile, etc., Co. v. Kneale, 51 Minn. 263, it was held that under Gen. St. 1878, ch. 34, tit. 1, § 4, and tit. 2, §§ 110, 118, a corporation organized as provided in title 2 is authorized by a majority vote in number and amount of its shareholders and stock shares to amend its articles of association, including the article which prescribes the nature of its corporate business in any respect, provided the amendment is germane to the subject-matter of the article to be amended, and could have been lawfully incorporated into the original articles of incorporation.

[5] Lauman v. L. V. R. Co., 30 Pa. St. 42; State v. Bailey, 16 Ind. 46.

[6] Mowry v. Ind., etc., R. Co., 4 Biss. (C. C.) 78.

[7] Bryan v. Board, 90 Ky. 322, 13 S. W. Rep. 276; Bedford R. Co. v. Bowser, 48 Pa. St. 29; State v. Sibley, 25 Minn. 387; Gifford v. N. J. R. Co., 10 N. J. Eq. 171; Rabe v. Dunlap, 51 N. J. Eq. 40, 25 Atl. Rep. 959.

then constitutes a contract which can not be impaired by future legislation.[1] Thus, a legislative grant of an exclusive right to supply gas to a municipality and its inhabitants, through pipes or mains laid in the public streets, and upon condition of the performance of the service by the grantee is a grant of a franchise vested in the state in consideration of the performance of a service, and after the performance of the service is a contract which can not be impaired by state legislation.[2] So, where the charter of a company authorized it to build and maintain a bridge across a river for the accommodation of the public in consideration for which it was given the right to charge tolls and provided that it should be unlawful for anyone to erect a bridge or establish a ferry within a distance of two miles on that river either above or below the bridge, it was held to be a contract within the meaning of the constitution of the United States.[3] These decisions rest upon the fact that the franchise granted was exclusive, but the mere grant of a charter to a private corporation does not prevent the state from making a similar grant to another corporation.[4] Thus, when a state grants a charter to a railway or canal company there is no implied contract between the corporation and the state that the state will not subsequently grant a similar franchise to another company which may render the franchise of the first corporation less valuable. In a famous case[5] it appeared that in the year 1650 the legislature of Massachusetts granted to the president of Harvard College "the liberty and power" to dispose of the ferry right from Boston to Charlestown for the benefit of the college. Under this act the college held the right till 1775, when the legislature incorporated a company by the name of "The Proprietors of the Charles River Bridge," for the purpose of erecting a bridge over the river "in the place where the ferry between

[1] Louisville, etc., Co. v. Citizens', etc., Co., 115 U. S. 683.

[2] New Orleans, etc., Co. v. La., etc., Co., 115 U. S. 650.

[3] The Binghamton Bridge, 3 Wall. (U. S.) 51.

[4] White River, etc., Co. v. Vt. Cent. R. Co., 21 Vt. 590.

[5] Charles River Bridge v. Warren Bridge, 11 Pet. (U. S.) 420, 431.

Boston and Charlestown was then kept." Under this charter the bridge company was required to pay to Harvard College the sum of two hundred pounds per year as compensation for what it might have received had the bridge not been erected. The bridge was constructed and operated until 1828, when the legislature incorporated a new company by the name of "The Proprietors of the Warren Bridge," for the purpose of erecting another bridge over the Charles river. The new bridge was erected within a few rods of the old one, and was to be surrendered to the state as soon as the proprietors were reimbursed for the expenses of building and supporting it, not to exceed six years from the time the company commenced to receive tolls. The bill for an injunction charged that the act for the erection of the Warren bridge impaired the obligation of the contract between the state and The Proprietors of the Charles River Bridge. The state court was evenly divided and therefore dismissed the bill, and the decision was affirmed by the supreme court of the United States. Before the hearing in the supreme court it was admitted that the Warren bridge proprietors had been reimbursed, and that the bridge was then the property of the state and a free bridge. After an extensive analysis of the grants and charter, Chief Justice Taney said: "The charter confers on them the ordinary faculties of a corporation for the purpose of building the bridge; and establishes certain rates of toll which the company is authorized to take; this is the whole grant. There is no exclusive privilege given to them over the waters of Charles river, above or below their bridge; no right to erect another bridge themselves, nor to prevent other persons from erecting one; no engagement from the state that another shall not be erected, and no undertaking not to sanction competition, nor to make improvements that may diminish the amount of its income. Upon all these subjects, the charter is silent, and nothing is said in it about a line of travel, so much insisted on in the argument, in which they are to have exclusive privileges. No words are used from

which an intention to grant any of these rights can be inferred; if the plaintiff is entitled to them, it must be implied, simply from the nature of the grant, and can not be inferred from the words by which the grant is made. * * * The inquiry, then, is, does the charter contain such a contract on the part of the state? Is there any such stipulation to be found in that instrument? It must be admitted on all hands that there is none; no words that even relate to another bridge, or to the diminution of their tolls, or to the line of travel. If a contract on that subject can be gathered from the charter, it must be by implication, and can not be found in the words used. Can such an agreement be implied? The rule of construction before stated is an answer to the question; in charters of this description no rights are taken from the public, or given to the corporation, beyond those which the words of the charter, by their natural and proper construction, purport to convey. There are no words which import such a contract as the plaintiffs in error contend for, and none can be implied."

§ 108. **Eminent domain.**—The property, franchises and contracts of corporations, like those of individuals, are subject to the sovereign power of eminent domain, and even the franchise of being a corporation may, under express legislative authority, be condemned for the benefit of another corporation.[1]

[1] Appeal of Pittsburgh Junction R. Co., 122 Pa. St. 511, 9 Am. St. Rep. 128, Ann. See also note to 4 Am. St. Rep. 404. Greenwood v. Freight Co., 105 U. S. 13, 22; New Orleans G. L. Co. v. La. G. Co., 115 U. S. 650; West River, etc., Co. v. Dix, 6 How. 507; Central, etc., Co. v. Lowell, 4 Gray 474; Richmond, etc., R. Co. v. Louisa. R. Co, 13 How. (U. S.) 71, 73; In re Minneapolis, etc., R. Co., 36 Minn., 481; Clarke v. Blackmar, 47 N. Y. 150; In re Providence, etc., R. Co., 17 R. I. 324, 21 Atl. Rep. 965; Amador, etc., Co v. Dewitt, 73 Cal. 483, 15 Pac. Rep. 74. In New Orleans, etc.,Co. v. Louisiana, etc., Co., 115 U. S. 650, Mr. Justice Harlan said: "If, in the judgment of the state, the public interest will be best subserved by an abandonment of the policy of granting exclusive privileges to corporations, other than railroad companies, in consideration of services to be performed by them for the public, the way is open for the accomplishment of that result, with respect to corporations whose contracts with the state are unaffected by that change in her organic law. The rights and franchises which

§ 109. **The police power.**—Corporations, like individuals, are subject to the police power of the state.[1] "The rights of all persons, whether natural or artificial, are subject to such legislative control as the legislature may deem necessary for the general welfare, and it is a fundamental error to suppose that there is any difference in this respect between the rights of natural and artificial persons. They both stand precisely upon the same footing. While personal liberty is guaranteed by the constitution to every citizen, yet, by disregarding the rights of others, one may forfeit not only liberty, but life itself. So a corporation by refusing to conform to the laws of its creation, or by so conducting its business affairs as to defeat the objects and purposes of its promoters and the design of the legislature in creating it, may forfeit its right to further carry on its business, and also its existence as an artificial being."[2]

A charter which confers the right to manufacture and sell malt liquors does not exempt the corporation from legislative control any more than an individual with the same powers. A statute which forbids the manufacture and sale of intoxicating liquors does not violate the constitution. "If the public safety or the public morals require the discontinuance of any form of manufacture or traffic, the hand of the legislature can not be stayed from providing for its discontinuance by any incidental inconvenience which individuals or corporations may suffer. All rights are held subject to the police power of the state." But property already manufactured can not be taken or destroyed without compensation.[3]

have become vested upon the faith of such contracts can be taken by the public, upon just compensation to the company, under the state's power of eminent domain." Woods Railway Law, I, pp. 661, 670. Lewis Eminent Domain, §§ 274, 275.

[1] Chicago, etc., Co. v. Needles, 113 U. S. 574; New York, etc., R. Co. v. Bristol, 151 U. S. 556; Eagle, etc., Co. v. Ohio, 153 U. S. 446; note to State v. Goodwill, 25 Am. St. Rep. 870–890; Thorp v. Rutland, etc., R. Co., 27 Vt. 141.

[2] Ward v. Farwell, 97 Ill. 593; Stone v. Mississippi, 101 U. S. 814; Beer Co. v. Massachusetts, 97 U. S. 25; Northwestern, etc., Co. v. Hyde Park, 97 U. S. 659; Mugler v. Kansas, 123 U. S. 623.

[3] Boston, etc., Co. v. Massachusetts, 97 U. S. 26.

§ 110. **Statutes affecting the remedy.**—The constitutional prohibition against the enactment of state laws impairing the obligation of contracts has no application to statutes modifying an existing remedy and providing a new and reasonably adequate one.

"The general doctrine of this court on this subject may be thus stated: In modes of proceeding and forms to enforce the contract the legislature has the control and may enlarge, limit, or alter them, providing it does not deny a remedy or so embarrass it with conditions or restrictions as seriously to impair the value of the right."[1]

§ 111. **Construction of corporate grants.**—Charters of private corporations are, when accepted, executed contracts, but the different provisions, when not clear and unambiguous, are subject to construction.[2] A grant to a corporation must be conveyed in clear and unmistakable terms. If the meaning of the words is doubtful they are to be taken most strongly against the corporation,[3] and especially is this true when the corporation is claiming some exclusive privilege or exemption.[4] Thus it is held that an enumeration of burdens to which a corporation is or may be subjected will not preclude the state from imposing others.[5] But the charter is the measure of the powers of a corporation,[6] and an enumeration of powers in the charter impliedly excludes all others.[7] "This enumeration of the purposes for which the corporation could acquire title to real estate must necessarily be held exclusive of all other purposes."[8] But such grants must be given a

[1] Penniman's Case, 103 U. S. 714; Hare's Am. Const. Law, I, p. 697.

[2] Turnpike Co. v. Illinois, 96 U. S. 63; Rice v. Railroad Co., 1 Black (U. S.) 358, 380.

[3] Holyoke Co. v. Lyman, 15 Wall. 511; N. W. F. Co. v. Hyde Park, 97 U. S. 659; Richmond R. Co. v. Louisiana R. Co., 13 How. 71.

[4] Omaha, etc., R. Co. v. Cable, etc., Co., 30 Fed. Rep. 324; Jersey City, etc., Co. v. Consumers', etc., Co., 40 N. J. Eq. 427; Ruggles v. Illinois, 108 U. S. 526; Tennessee v. Whiteworth, 117 U. S. 139, 148; The Railroad Commission Cases, 116 U. S. 326.

[5] Railway Co. v. Philadelphia, 101 U. S. 528; Hare's Am. Const. Law, p. 666.

[6] Bank, etc., v. Earl, 13 Pet. 588; Rochester, etc., Co. v. Martin, 13 Minn. 59, Gil. 51.

[7] Thomas v. Railway Co. 101 U. S. 71.

[8] Case v. Kelley, 133 U. S. 21; F. & M. Bank v. Baldwin, 23 Minn. 198.

reasonable construction, and powers fairly incidental to the objects of the corporation are implied.[1]

§ 112. **Taxation of corporations.**—Corporations, like individuals, are subject to the taxing power of the state. In taxing a corporation, the state must observe those general principles by which all exercise of the sovereign power of taxation is to be tested. The contractual relation existing between the corporation and the state does not, in the absence of an express exemption from taxation, limit the taxing power. In the absence of constitutional limitations, the state may impose what amounts to double taxation upon corporations.[2] In order to determine whether double taxation results, it is necessary to analyze the elements of taxable values to be found in corporations. These are, ordinarily, franchises, capital stock in the hands of the corporation, corporate property, and shares of the capital stock in the hands of individuals. Each is, under some circumstances, an appropriate subject for taxation. And it is within the power of the state, when not restrained by constitutional limitations, to assess taxes upon them in a way to subject the corporation or the stockholders to double taxation. The intent to impose double taxation is, however, never to be presumed.[3]

The capital stock is thus distinguished from shares which represent the interest of individual shareholders.[4] "The interest of a shareholder," says Mr. Justice Nelson,[5] "entitles him to participate in the net profits earned by the bank in the employment of its capital during the existence of its charter,

[1] Carothers v. Philadelphia Co., 118 Pa. St. 468; Wisconsin, etc., Co. v. Oshkosh, 62 Wis. 32; State v. Payne, 129 Mo. 468; Ross-Meehan, etc., Co. v. So. M., etc., Co., 72 Fed. Rep. 957; Parker v. Railway Co., 7 Man. & G. 288.

[2] State v. Whitworth, 117 U. S. 129; Fall River, v. Cornes, 125 Mass. 567; Railroad Tax Cases, 13 Fed. Rep. 722; Board v. Montgomery, etc., Co., 64 Ala. 269; Pittsburgh, etc., R. Co. v. Com., 66 Pa. St. 77. Attention is called to an article on the Taxation of Corporations, by F. W. Taussig, in Pol. Sci. Quarterly for March, 1899.

[3] State v. Whitworth, 117 U. S. 129; Salem, etc., v. Danvers, 10 Mass. 514. See note 4, § 120, *infra*. See Wilgus' Cases.

[4] Delaware R. Tax Case, 18 Wall, 206; Mfgrs., etc., Co. v. Loud, 99 Mass. 146; Farrington v. Tennessee, 95 U. S. 679; Com. v. Building, etc., 90 Va. 790; Porter v. Rockford, etc., R. Co., 76 Ill. 561.

[5] Van Allen v. Assessors, 3 Wall. (U. S.) 573.

in proportion to the number of his shares; and upon its dissolution or termination, to his proportion of that which may remain after the payment of its debts. This is a distinct, independent interest or property held by the shareholder like any other property that may belong to him." A tax upon the property or capital of a corporation, as distinguished from its franchises, is not double taxation.[1]

§ 113. **Situs of taxable property.**—No general principle of law is better settled than that the legislative power of a state extends to all the property within its borders, and that only so far as the comity of that state allows, can such property be affected by the law of any other state. The old rule that personal property was subject to the law of the owner's domicile has in modern times yielded somewhat to the *lex situs*, the law of the place where the property is kept and used. For purposes of taxation personal property may be separated from its owner, and he may be taxed on its account at the place where it is situated, although not the place of his own domicile. This is true although the owner is not a citizen or a resident of the state which imposes the tax.[2] Thus, the shares of stock of a corporation may be taxed at the place of the domicile of the corporation, that is, the place of business of the corporation, without reference to the residence of the stockholder.[3] And at the same time the state in which the owner of the stock resides, may also tax the shares at the place of his residence.[4] Tax laws, however, have no extraterritorial operation, and the power of taxation by the state is limited to the jurisdiction of the state.[5] A state can not, therefore, tax the

[1] Farrington v. Tenn., 95 U. S. 679, and cases cited above.

[2] Lane Co. v. Oregon, 7 Wall. (U. S.) 71; Railroad Co. v. Pa., 15 Wall. (U. S.) 300; Railroad Co. v. Peniston, 18 Wall. (U. S.) 5; Tappan v. Merchants' Bank, 19 Wall. 490; Marye v. B. & O. R. Co., 127 U. S. 117.

[3] Tappan v. Merchants' Bank, 19 Wall. 490; South Nashville, etc., Co. v. Morrow, 87 Tenn. 406; St. Albans v. National, etc., Co., 57 Vt. 68; N. C. R. Co. v. Comm., 91 N. C. 454.

[4] Sturges v. Carter, 114 U. S. 521; Bradley v. Bauder, 36 Ohio St. 28. See Ogden v. St. Joseph, 90 Mo. 522, 3 S. W. Rep. 25.

[5] Comm. v. Standard, etc., Co., 101 Pa. St. 119.

entire track and equipment or the total capital stock of a railroad corporation whose track lies partly in another state. It can tax only the property which is within the state or that proportion of the capital stock which is represented by such property.[1] There is nothing in the constitution or laws of the United States which prevents a state from taxing personal property which is within its territorial limits, although it is employed in interstate or foreign commerce.[2] The state may impose a tax on the capital stock of a corporation computed on a percentage of the dividends made or declared. Thus, in order to ascertain the proportion of the Pullman Palace Car Co.'s property upon which it should pay taxes in Pennsylvania, the state took as the basis of assessment such proportion of the capital stock of the company as the number of miles over which it ran cars in the state bore to the whole number of miles in that and other states over which it ran in that and in other states. "This," says the supreme court,[3] "was a just and equitable method of assessment; and, if it were adopted by all the states through which these cars ran, the company would be assessed on the whole value of its capital stock, and no more."

§ 114. **Restrictions imposed by the federal constitution.**— The taxing power of the United States is derived from the express grants contained in the constitution, while the power of the states is limited only by the restrictions imposed upon it by the federal or state constitutions. The federal constitution provides that "No state, without the consent of congress, shall lay any impost or duties on imports or exports, except what shall be absolutely necessary for executing its inspection laws." Other restrictions which affect the power of taxation are found in

[1] Pullman, etc., Co. v. Penn., 141 U. S. 18; Western, etc., Co. v. Taggart, 163 U. S. 1; State v. Auditor-Gen., 46 Mich. 226. But the supreme court of the United States has held that the capital stock of a corporation represents both its tangible and intangible property, such as franchises, contracts, privileges and good will; and when the tangible property is scattered in many states, as in case of express companies, the situs of this intangible property is not simply at its home office, but wherever its tangible property is, and its work done. Adams Ex. Co. v. Ohio State Auditor, 166 U. S. 185, s. c. 165 U. S. 194 and 255; 6 A. & E. Corp. Cas. N. S. 404.

[2] Delaware R. Tax, 18 Wall. 206; Telegraph Co. v. Texas, 105 N. S. 460; Western, etc., Co. v. Att'y-Gen., 125 Mass. 530.

[3] Pullman, etc., Co. v. Penn., 141 U. S. 18. As a basis of assessment, this was approved in Mayre v. B. & O. R. Co., 127 U. S. 117; Western, etc., Co. v. Mass., 125 U. S. 530; State R. Tax Cases, 92 U. S. 575.

the provision of the fourteenth amendment to the constitution which forbid any state to deny to any person within its jurisdiction the equal protection of its laws. Corporations are within the meaning of this provision, and hence all domestic corporations must be treated alike, and must be granted all privileges and exemptions which are granted to natural persons within the state.[1] The state may, however, discriminate between domestic and foreign corporations.[2] The provision of the constitution which reserves to congress exclusive control over interstate commerce, prevents the state from imposing any tax which amounts to an interference with or control over commerce between the states. Thus, a state can not tax a foreign railroad corporation upon its business within the state which is exclusively interstate commerce,[3] and a tax upon gross receipts is not valid.[4] So, the state may tax the vehicles of commerce,[5] but a tax on freight carried from state to state is invalid.[6]

§ 115. **Federal agencies.**—The agencies of the national government are beyond the reach of the taxing power of the state. The power to tax involves the power to trammel and destroy. This principle, established by McCulloch v. Maryland,[7] is no longer controverted. Thus, the state can not tax a franchise granted to a corporation by congress,[8] and it is held that this extends to the capital stock of a corporation which was issued for a patent-right granted by the United States.[9] A distinction is made between a tax upon the operations of a federal agency and a tax upon the property which belongs to the agency, when the tax in no way impairs its efficiency.[10]

[1] Santa Clara Co. v. Southern, etc., R. Co., 118 U. S. 394.

[2] Ducat v. Chicago, 48 Ill. 172.

[3] People v. Wemple, 138 N. Y. 1. See Lehigh, etc., R. Co. v. Pennsylvania, 145 U. S. 192.

[4] Philadelphia & S. S. Co. v. Pennsylvania, 122 U. S. 326, questioning, or overruling, State Tax Cases, 15 Wall. (U. S.) 284; Railway Co. v. Weber, 96 Ill. 443. But an excise tax on a foreign corporation's privilege of exercising its franchises in a state, graduated in proportion to the gross earnings per mile for the whole road, has been held to be valid, and not to be a tax on gross earnings. Maine v. R. Co., 142 U. S. 217. See, however, dissenting opinion of Justices Bradley, Lamar and Brown.

[5] Wiggins, etc., Co. v. East St. Louis, 107 U. S. 365.

[6] State Freight Tax, 15 Wall. (U. S.) 233.

[7] 4 Wheat. (U. S.) 316.

[8] California v. Pac. R. Co., 127 U. S. 1.

[9] Comw. v. Phila. Co., 157 Pa. St. 527.

[10] Railroad Co. v. Peniston, 18 Wall.

§ 116. **State taxation of national banks.**—The power of the states to tax national banks is conferred by the act of congress of July 3, 1864.[1] This act subjects the shares of national banks in the hands of shareholders to taxation by the state under the limitation contained therein, without regard to the fact that a part or the whole of the capital of the bank is invested in national securities declared by the statute to be exempt from taxation by or under state authority. The question arose under an act of a state legislature which provided that shares in any national bank held by any person should be "included in the valuation of the personal property of such person or body corporate in the assessment of taxes in the town or ward where such banking association is located and not elsewhere," but did not provide that the tax imposed should not exceed the rate imposed upon any of the banks organized under the authority of the state. The act was held invalid, it appearing that no tax whatever had been laid on the shares of state banks, although there was a tax on their capital.[2] This decision was followed in a subsequent case,[3] where it was said that if the rate of taxation on such shares is the same as or not greater than upon the moneyed capital of the individual citizen, which is subject or liable to taxation, the shares are taxed in conformity with the provisions of the act which says that they may be assessed, "but not at a greater rate than is assessed upon other moneyed capital in the hands of individual citizens of the state." As in the former case, in valuing these shares, no deduction was made on account of the capital of the bank invested in United States securities. In the valuation of the personal estate of individuals, however, the securities held and owned by them were deducted and the tax assessed on the balance, and like deductions were made from the capital of insurance companies. It was argued that the assessment upon the shares of the relator was at a greater rate than upon the per-

(U. S.) 5; Central, etc., Co. v. Calif., 162 U. S. 91; Adams, etc., Co. v. Ohio, 165 U. S. 194.

[1] U. S. Rev. St., § 5219. See Boyer v. Boyer, 113 U. S. 689.

[2] VanAllen v. Assessor, 3 Wall. (U. S.) 573; People v. Comrs. 94 U. S. 415.

[3] People v. Comrs., 4 Wall. (U. S.) 244.

sonal property of individual citizens. The answer is, said the court, that upon a true construction of this clause of the act, the meaning and intent of the law makers were that the rate of taxation of the shares should be the same or not greater than upon the moneyed capital of the individual citizen which is subject or liable to taxation. That is, no other or greater percentage of tax in the valuation of shares should be levied than upon the moneyed taxable capital in the hands of the citizen.

The act of congress does not require perfect equality between state and national banks, but only that the system of taxation in a state shall not work a discrimination favorable to its own citizens and corporations and unfavorable to the holders of shares in national banks. If the state statute creating a system of taxation does not on its face discriminate against a national bank, and there is neither evidence of a legislative intent to make such discrimination, nor proof that the statute makes an actual and material discrimination, the act will not be held invalid.[1]

§ 117. **Meaning of "other moneyed capital."**—In a leading case[2] the court said that "moneyed capital in the hands of individual citizens" does not necessarily embrace shares of stock held by them in all corporations whose capital is employed according to their respective corporate powers and privileges in business carried on for the pecuniary profit of shareholders, although shares in some corporations, according to the nature of their business, may be such moneyed capital. The rule and test of this difference is not to be found in that quality attached to shares of stock in corporate bodies generally whereby the certificates of ownership have a certain appearance of negotiability."

After a discussion of the object of the law, the court continues: "Applying this rule of construction, we are led in the first place to consider the meaning of the words, 'other moneyed

[1] Davenport Bank v. Board, etc., 123 U. S. Rep. 83; Hepburn v. School Directors, 23 Wall. (U. S.) 480; Adams v. Nashville, 95 U. S. Rep. 19.

[2] Mercantile Bank v. New York, 121 U. S. Rep. 138.

capital,' as used in the statute. Of course, it includes shares in national banks; the use of the word 'other' requires that. * * * But '*moneyed capital*' does not mean all capital the value of which is measured in terms of money. * * * Neither does it necessarily include all forms of investment in which the interest of the owner is expressed in money. Shares of stock in railroad companies, mining companies, manufacturing companies and other corporations are represented by certificates showing that the owner is entitled to an interest, expressed in money value, in the entire capital and property of a corporation, but the property of a corporation which constitutes its invested capital may consist mainly of real and personal property, which in the hands of individuals no one would think of calling moneyed capital; and its business may not consist of any kind of dealing in money or commercial representative of money. * * * Credits, money loaned at interest, and demands against persons or corporations, are more purely representative of moneyed capital than personal property, so far as they can be said to differ.''

Deposits in savings banks are moneyed capital in the hands of individuals, but they are not within the meaning of the act of congress in such a sense as to require that, because they are exempt from taxation, the shares of stock in national banks must also be exempt.[1] Shares in a national bank held by another national bank are subject to taxation.[2] Money invested in corporation or in individual enterprises that carry on the business of railroads, manufacturing, mining investments, and investments in mortgages, do not come into competition with national banks, and do not come within the provisions of the statute. So, insurance stocks may be taxed on income instead of value, and deposits in savings banks and money belonging to charitable institutions may be exempted without

[1] Mercantile Bank. v. New York, 121 U. S. 138; Davenport Bank v. B. of Eq. 123 U. S. 83; Hepburn v. School Directors, 23 Wall. 480; Bank of Redemption v. Boston, 125 U. S. 60. As to the claim that a state statute violates the fourteenth amendment, see Prov. Inst. for Sav. v. Boston, 101 Mass. 575.

[2] Mercantile Bank v. New York, 121 U. S. 138.

infringing the statute.[1] Exemptions from taxation granted before the act of congress was passed do not create such inequalities as are contemplated by the law. Congress must have acted with the knowledge that the states might in certain instances have contracted themselves out of the power to tax certain institutions; hence, the fact that the shares of national banks are taxed two per cent., while under an old law the state could, and did, tax the shares in a certain state bank at one per cent., does not invalidate the tax on the shares of the national bank.[2] Exemption from taxation of interest-bearing municipal bonds does not affect the validity of the national bank stock tax.[3]

§ 118. **Telegraph companies.**—In respect to foreign and interstate business, a telegraph company is an instrument of commerce, and subject to the regulating power of congress.[4] If it accepts the provisions of the statute,[5] it becomes an agent of the government so far as the business of the government is concerned, and a state statute which imposes a specific tax on each message which is transmitted beyond the state, or which an officer of the United States sends over its line, on public business, is unconstitutional.[6] No tax can be imposed by the state upon messages sent by such a company, or upon the receipts derived therefrom, where the communication is carried either into the state from without or from within the state to another state. A tax may, however, be levied upon all messages carried and delivered exclusively within the state. The foundation of this principle is that messages of the former class are elements of commerce between the states and not subject to legislative control of the states, while the latter class

[1] Aberdeen Bank v. Chehalis Co., 166 U. S. 440.

[2] Lionberger v. Rouse, 9 Wall. (U. S.) 468.

[3] Adams v. Nashville, 95 U. S. 19; Mercantile Bank v. New York, 121 U. S. 138.

[4] Pensacola, etc., Co. v. Western, etc., Co., 96 U. S. 1, Wilgus' Cases.

[5] Rev. St. U. S., §§ 5263-5268.

[6] Telegraph Co. v. Texas, 105 U. S. 460. "As to the government messages, it is a tax by the state on the means employed by the government of the United States to execute its statutory powers, and therefore void. It was so decided in McCulloch v. Maryland, 4 Wheat. 316, and has never been since doubted."

are elements of internal commerce solely within the limits and jurisdiction of the state, and therefore subject to its taxing power.[1] The state or a municipality may impose a license fee under certain conditions, as this is an ordinary exercise of the police power.[2] A city ordinance imposing a license fee upon a telegraph company, which had accepted the provisions of the act of congress, upon business done exclusively in the city, and not including any business done to or from any points without the state, and not including business done for the government of the United States, its officers or agents, is an exercise of the police power, and not an interference with interstate commerce.[3] A municipal charge for the use of the streets by a telegraph company erecting its poles therein is not a privilege or license tax. "The amount to be paid is not graduated by the amount of the business, nor is it a sum fixed for the privilege of doing business. It is more in the nature of a charge for the use of property belonging to the city, that which may properly be called rental. 'A tax is a demand of sovereignty; a toll is a demand of proprietorship.'"[4]

§ 119. **Other agencies of commerce.**—A railroad company which is a link in a through line of road by which passengers and freight are carried into a state from another state, and from the state into other states, is engaged in the business of interstate commerce, and a tax imposed by such state upon the corporation owning the road, for the privilege of keeping an office in the state, it being a corporation created in another state, is a tax upon commerce, and invalid. The office was maintained because of the necessities of the interstate business of the company, and for no other purpose. A tax upon

[1] Western, etc., Co. v. Alabama, 132 U. S. 472; Telegraph Co. v. Texas, 105 U. S. 460; Telegraph Co. v. Massachusetts, 125 U. S. 530; Ratterman v. Western, etc., Co., 127 U. S. 411; Leloup v. Mobile, 127 U. S. 640; Fargo v. Michigan, 121 U. S. 230; Pacific, etc., Co. v. Seibert, 142 U. S. 339; Postal, etc., Co. v. Charleston, 153 U. S. 692.

[2] Wiggins, etc., Co. v. E. St. Louis, 107 U. S. 365.

[3] Postal, etc., Co. v. Charleston, 153 U. S. 692.

[4] St. Louis v. Western, etc., Co., 148 U. S. 96. This same distinction is made in taxing rentals received by one railroad company from another engaged in interstate commerce. See N. Y., L. E. & W. R. Co. v. Pennsylvania, 158 U. S. 431; State Freight Tax Case, 15 Wall. (U. S.) 232.

it was therefore a tax upon one of the means or instrumentalities of the company's interstate commerce, and as such was in violation of the commercial clause of the constitution.[1] An act requiring a license from the agent of an express company is invalid as a regulation of interstate commerce, in so far as it applies to a corporation of another state engaged in that business.[2]

§ 119a. **Exemption from taxation.**—The state may exempt certain property of a corporation or an individual from the burden of taxation, and if the grant of the privilege is supported by a consideration it can not be withdrawn without impairing the obligation of the contract between the state and the beneficiary.[3] The property used by railway corporations in their business is often exempted from general taxation, and in lieu thereof, or as a consideration therefor, the corporation pays a tax upon its gross receipts.[4] Exemption of all the property of a railroad corporation includes its rolling stock and franchises. The exemption of the capital stock of a corporation does not exempt the shares in the hands of the stockholders.[5] When a corporation is exempt from taxation, a statute which purports to tax the shares in the hands of the stockholders, but requires the corporations to pay the tax and collect it out of money which may become due the stockholders, without reference to there being any profits out of which to pay it, is invalid.[6] Exemption from taxation is never presumed, as the

[1] Norfolk, etc., R. Co. v. Pennsylvania, 136 U. S. 114, citing Gloucester, etc., Co. v. Pennsylvania, 114 U. S. 196; McCall v. California, 136 U. S. 104.

[2] Crutcher v. Kentucky, 141 U. S. 47.

[3] Jefferson Branch Bank v. Skelly, 1 Black (U. S.) 436; Farrington v. Tennessee, 95 U. S. 679; No. Mo. R. Co. v. Maguire, 20 Wall. (U. S.) 46; Memphis, etc., Co. v. Shelby Co., 109 U. S. 398; Asylum v. New Orleans, 105 U. S. 362; Nichols v. Northampton Co,, 42 Conn. 103; Neustadt v. Railroad Co., 31 Ill. 484.

It has been held that the state could not grant an irrevocable exemption from taxation. Skelly v. Bank, 9 Ohio 606 (overruled, however, by Jefferson Br. Bank v. Skelly, 1 Black (U. S.) 436); Mott v. Railroad Co., 30 Pa. St. 9.

[4] St. Paul v. St. Paul, etc., R. Co., 23 Minn. 469.

[5] Van Allen v. Assessors, 3 Wall. (U. S.) 573; Nat. Bank v. Com., 9 Wall. (U. S.) 353.

[6] Salt Lake City v. Hollister, 118 U. S. 256.

rule is imperative that the relinquishment of the taxing power is never to be presumed.[1] Such grants are strictly construed against the grantee. Thus, a general exemption from taxation will not be so construed as to exempt from a local assessment.[2] So it is held that when capital stock is exempt the property into which it was converted is not exempt.[3] Where one corporation succeeds to the rights and powers of another, an exemption from taxation enjoyed by the first corporation will not pass to the second unless such was clearly the intention as evidenced by the acts of the state.[4] But where two corporations unite or become consolidated under the authority of law, the presumption is, until the contrary appears, that the consolidated company has all the powers and privileges and is subject to all the restrictions and liabilities of those out of which it was created.[5] Hence, where two railroad companies whose shares are by a state statute exempt from taxation within the state, and a third company, created under the laws of another state, and whose road is in the latter state, become merged into a new company, and issue shares of the new company in exchange for shares of the old company, the right of exemption from taxation in the first state passes into the new shares, and each of them, unless a law of the first state makes provision to the contrary.[6] In order that the consolidated corporation may succeed to the privilege of exemption from taxation it must be

[1] Vicksburg, etc., R. Co. v. Dennis, 116 U. S. 665; Delaware R. Tax, 18 Wall. (U. S.) 206.

[2] Elliott Pub. Co., § 119, and cases there cited.

[3] Memphis, etc., Co. v. Gaines, 97 U. S. 697.

[4] Wilmington, etc., Co. v. Alsbrook, 146 U. S. 279; Annapolis, etc., R. Co. v. Comis, 103 U. S. 1. *Contra*, Nichols v. Railroad Co., 42 Conn. 193.

[5] Tenn. v. Whitworth, 117 U. S. 139, per C. J. White, citing Tomlinson v. Branch, 15 Wall. 460; Branch v. Charleston, 92 U. S. 677; County of Scotland v. Thomas, 94 U. S. 682; Railroad Co. v. Maine, 96 U. S. 499; Green Co. v. Conness, 109 U. S. 104; Phila., etc., R. Co. v. Md., 10 How. (U. S.) 376. But compare Pearsall v. Great Northern R. Co., 161 U. S. 646.

[6] Tennessee v. Whitworth, 117 U. S. 139. See, however, Keokuk & W. R. Co. v. Missouri, 152 U. S. 301, where the true rule is said to depend upon the effect of the consolidation—if a really new company (and not a mere merger of the old) comes into existence, and the old companies are dissolved, then the exemptions of the old companies do not pass to the new. The leading case on this point is Railroad Co. v. Georgia, 98 U. S. 359.

clearly made to appear that such was the legislative intent.[1] The new company holds the immunities of the old companies distributively; that is, whatever privileges and immunities the former companies possessed inure to the benefit of the new corporation to the extent of the property owned by each of the former companies at the time of the consolidation.[2] A general exemption clause applies only to property which is reasonably necessary to carry out the purposes of the corporation.[3] The legislature may reserve the power to revoke a grant of exemption from taxation.[4] Under such a reserve power the rate of taxation may be increased.[5]

[1] Railroad Co. v. Maryland, 10 How. (U. S.) 376; The Delaware R. Tax, 18 Wall. (U. S.) 206; Railroad Co. v. Missouri, 152 U. S. 301.

Where corporations are consolidated, exemption from taxation does not pass to the new corporation, unless such is clearly the legislative intention. See Adams v. Yazoo, etc., Co. (Miss.), 24 So. Rep. 317.

[2] Tomlinson v. Branch, 15 Wall. (U. S.) 460; Tenn. v. Whitworth, 117 U. S. 139. See, particularly, State v. Maine, etc., R. Co., 66 Me. 488, 514.

[3] Railroad Co. v. Berks Co., 6 Pa. St. 70; Lehigh, etc., Co. v. Northampton Co., 8 Watts & S. (Pa.) 334.

[4] Tomlinson v. Jessup, 15 Wall. (U. S.) 454.

[5] Union Pac. R. Co. v. Phila., 101 U. S. 528. For purposes of taxation the franchises of a corporation may be distinguished from its other property. The practical difficulty in the way of the taxation of franchises has been to find an equitable method of determining the value of the franchise. A proper method of valuation is to take the market or actual value of all the indebtedness, exclusive of debts for current expenses, and the market or actual value of all the stock of every kind issued, and the total will be the value of all the assets of the corporation. From this deduct the actual or market value of all the tangible property in its possession, and there remains the value of the intangible property, or the franchise. This method is recognized by the laws of Connecticut, New Jersey, Indiana, Illinois and other states. In Talor v. Secor, 99 U. S. 575, Mr. Justice Miller says: "It is therefore obvious that when you have ascertained the current cash value of the whole funded debt, and the current cash value of the entire number of shares, you have, by the action of those who above all others can best estimate it, ascertained the true value of the road, all its property, its capital stock and its franchises. For these are all represented by the value of its bonded debt, and of the shares of its capital stock." See an article on "Taxation of Public Franchises," by John Ford, in North American Review, for June, 1899.

CHAPTER 5.

FRANCHISES AND PRIVILEGES.

§ 120. The nature of a franchise.
121. Illustrations of franchises—Conditions—Grant of right to use street for railway purposes.
122. Illustrations—Nature of rights acquired.
123. The franchise of being a corporation.
124. In whom franchises vests.
§ 125. The sale and transfer of franchises.
126. Corporations charged with public duties.
127. Transfer under legislative authority—Construction.
128. Franchises pertaining to use of particular property.
129. Forfeiture of franchises.
130. Constitutional protection of franchises.

§ 120. **The nature of a franchise.**—Some confusion exists in the decisions as to the meaning of the word franchise. It is sometimes given a broad significance and made to cover all the rights, powers and privileges of corporations. Properly, however, a distinction must be made between a franchise, a power and a mere personal privilege. A franchise is a special privilege conferred by the sovereign power upon a natural or artificial person, which does not belong to a person as of common right.[1] As defined by Chief Justice Taney:[2] "Franchises are special privileges conferred by government upon individuals, and which do not belong to the citizens of the country, generally, of common right. It is essential to the character of a franchise that it should be a grant from the sovereign authority, and in this country no franchise can be held which is not derived from the law of the state." Another learned judge said:[3] "To be a franchise, the right possessed must be such

[1] Green v. Knife, etc., Co., 35 Minn., 155. A franchise is a special privilege emanating from the sovereign power and owing its existence to a grant or to a prescription pre-supposing a grant. Wilmington, etc., Co. v. Evans, 166 Ill. 548, 46 N. E. Rep. 1083. See statement of Mr Justice Field in Morgan v. Louisiana, 93 U. S. 223.

[2] Bank, etc., v. Earl, 13 Peters (U. S.) 595. See, also, Spring Valley W. W. v. Schottler, 62 Cal. 73; State v. Scougal, 3 S. D. 55, 15 L. R. A. 477, 51 N. W. Rep. 858.

[3] Mitchell, J., in State v. Minn., etc., Co., 40 Minn. 213. See, also, Memphis R. Co. v. Comrs., 112 U. S. 619.

as can not be exercised without the express permission of the sovereign power—a privilege or immunity of a public nature which can not be legally exercised without a legislative grant. It follows that the right, whether existing in a natural or artificial person, to carry on any particular business is not necessarily or usually a franchise." In an important case in the supreme court, Mr. Justice Bradley said:[1] "What is a franchise? Under the English law Blackstone defines it as 'a royal privilege or branch of the king's prerogative subsisting in the hands of a subject.' Generalized and divested of the special form which it assumed under a monarchical government, based on feudal traditions, a franchise is a right, privilege or power of public concern, which ought not to be exercised by private individuals at their mere will and pleasure, but should be reserved for public control and administration, either by the government directly, or by public agents, acting under such conditions and regulations as the government may impose in the public interest, and for the public security. Such rights and powers must exist under every form of society. They are always educed by the laws and customs of the community. Under our system their existence and disposal are under the control of the legislative department of the government, and they can not be assumed or exercised without legislative authority No private person can establish a public highway, or a public ferry, or railroad, or charge tolls for the use of the same without authority from the legislature direct or derived. These are franchises. No private person can take another's property, even for public use, without such authority; which is the same as to say, that the right of eminent domain can only be exercised by virtue of a legislative grant. This is a franchise. No persons can make themselves a body corporate and politic without legislative authority. Corporate capacity is a franchise."

§ 121. **Illustrations of franchises — Conditions — Grant of right to use street for railway purposes.**—The illustrations of

[1] California v. Central, etc., Co., 127 U. S. 40. For distinction between a franchise and a mere monopoly, see note, 4 L. R. A. 616.

franchises which are granted to corporations and individuals in modern times might be extended indefinitely. The common franchises, the right to be a corporation, to exercise the power of eminent domain, to establish a ferry or bridge and charge tolls, are referred to in the preceding section. The authorities are conflicting on the question whether an ordinance granting the consent of a municipality to a street railway company to the use of a street for the purpose of laying tracks is a franchise or merely a license. In one line of cases it is held that where a street railway company is incorporated under an act of the legislature, with power to construct, maintain and operate a railroad in a city, upon obtaining the consent of the city in such manner and under such conditions as the city may impose, and the city by ordinance grants the privilege of constructing and operating the same upon a certain street, the grant is a mere license, and not a franchise.[1] Thus an ordinance granted to a railway company the right and privilege of laying its tracks and operating its road along certain streets upon certain conditions,[2] and provided that "upon the failure of the company to comply with any condition herein named, the said council shall have the power, which it hereby expressly reserves, to repeal the ordinance and revoke the consent hereby given." The company failed to perform one of the conditions, and the council passed a repealing ordinance. It was held that the company had a license, and not a franchise, and that the repealing ordinance was valid.[3]

Upon the general principle that the council can not deprive its successor of legislative power by the enactment of an irrepealable ordinance, it was held that an ordinance giving a street

[1] Chicago, etc., R. Co. v. People, 73 Ill. 541; Chicago Board of Trade v. People, 91 Ill. 80; Belleville v. Citizens', etc., Co., 152 Ill. 171, 26 L. R. A. 681.

[2] That the legislature may impose conditions when granting a franchise, see State v. Spartanburg, etc., Co. (S. C.), 28 S. E. Rep. 145; San Diego, etc., Co. v. San Diego (Cal.), 50 Pac. Rep. 633, 38 L. R. A. 460; Grannan v. Westchester, etc., Assn., 153 N. Y. 449.

[3] Belleville v. Citizens', etc., Co., 152 Ill. 171, 26 L. R. A. 681. But a later Illinois case holds that authority to so use the streets is not a mere license, or private contract, but is something more, a franchise that carries with it a public duty enforceable by mandamus. The People v. Suburban R. Co., 178 Ill. 594.

railway company the right to lay a double track in a street might be repealed and the right limited to a single track. The company in such case has no claim against the city for the value of improvements made after notice of the intention of the city to repeal the ordinance.[1]

The privilege to use the streets for railway purposes, when granted by an ordinance, if granted on an adequate consideration and accepted by the grantee, may be a valid and binding contract. Although the ordinance has been accepted and acted on, the resulting contract may be subject to rescission, because of the failure of the corporation to observe conditions which were attached to the grant. This failure does not, however, avoid the contract. It merely puts it in the power of the city to rescind it.[2]

[1] Lake Roland, etc., R. Co. v. Baltimore, 77 Md. 352, 20 L. R. A. 126; Baltimore v. Baltimore, etc., Co., 166 U. S. 679. The change from a double to a single track was a reasonable regulation concerning the use of the street.

The legislative action of a municipal corporation can not be enjoined. Hence, a city council will not be enjoined from passing an ordinance allowing another gas company to lay pipes in the streets, because the city has already granted an exclusive franchise to lay and maintain gas pipes to the complainant. Montgomery, etc., Co. v. City Council (Ala.), 4 L. R. A. 616.

[2] In Belleville v. Citizens', etc., R. Co., 152 Ill. 171, 26 L. R. A. 681-685, the court said: "These failures on the part of the appellee did not of themselves avoid the contract, but they put it in the power of the city to rescind it. It is entirely competent for parties to a contract to introduce into it a provision that if one of them fails to fulfill certain specified terms, the other shall be entitled to treat the agreement as at an end. There is a difference between this mode of discharging a contract, and that by breach. When the parties have agreed that one of them shall have an option to dissolve the contract, if certain of its terms are not observed, upon the non-fulfillment of the specified terms, the party may exercise his option; and if he elects to treat the contract as at an end it will be discharged. But when a term of a contract is broken, and there is no agreement that the breach of that term shall operate as a discharge, it is always a question for the courts to determine whether or not the default is in a matter which is vital to the contract; for if it is not, the contract will not be discharged. 3 Am. & Eng. Enc. of Law, p. 893, note 5; Head v. Tattersall, L. R. 7 Exch. 7.

"The contract at bar was of the kind first mentioned above. It contained provisions which made it determinable under certain circumstances at the election of the city, and how was the city to indicate its election to avoid the contract? Manifestly, by passing an ordinance repealing the ordinance that constituted the contract, and revoking all the rights and privileges granted thereby, and by notifying ap-

§ 122. **Illustrations—Nature of rights acquired.**—There is high authority for the position that a grant to a railway company by a city of the right to use the streets for its tracks constitutes an easement, and that the right granted thereby is an interest in realty, being an incorporeal hereditament.[1] In New York corporate franchises are taxed as real property. A recent writer of authority says: "The right granted by a municipality to use its streets is frequently called a franchise, but it is a franchise in the secondary rather than the primary sense of the term. Indeed, it seems to us that it is more in the nature of a license, which may be revoked at any time prior to its acceptance, and which vests no right in the licensee until it is 'accepted and used.'[2] A valid grant of such right by ordinance, however, upon an adequate consideration, when accepted and acted upon by the grantee, becomes an irrevocable and binding contract.[3] Unless the right to repeal or amend is reserved, the city can not revoke the ordinance nor, by a subsequent ordinance, without the consent of the company, impose upon it further and additional burdens.[4] But the right to do so may be reserved."[5]

In Wisconsin it is held that a franchise given by a city to a street railway company is something more than a mere easement or license to use the streets for the time and in the manner specified in the ordinance, and more than a contract between the public and the railway company when the ordinance has

pellee to remove its tracks, switches and turnouts from the streets of the city."

[1] Detroit, etc., R. Co. v. City of Detroit, 64 Fed. Rep. 628, 26 L. R. A. 667; People v. O'Brien, 111 N. Y. 1, 2 L. R. A. 255, 7 Am. St. Rep. 684. See New Orleans, etc., R. Co. v. Delamore, 114 U. S. 501, where it was held that a right of way for railway tracks in a street is a franchise which can be mortgaged and transferred.

[2] Atchison, etc., R. Co. v. Nave, 38 Kan. 744, 5 Am. St. Rep. 804, Ann.; People v. Mutual, etc., Co., 38 Mich. 154; City of Belleville v. Cit., etc., R. Co., 152 Ill. 171, 26 L. R. A. 681; Galveston, etc., R. Co. v. Gulf City, etc., R. Co., 63 Texas 529; Detroit v. Detroit, etc., R. Co., 37 Mich. 558; Booth Street Railways, § 10.

[3] City of St. Louis v. Western Union, etc., Co., 63 Fed. Rep. 68.

[4] People v. Chicago, etc., R. Co., 118 Ill. 113; Electric R. Co. v. Common Council, 84 Mich. 257; Western, etc., Co. v. Citizens', etc., R. Co., 128 Ind. 525.

[5] Elliott Railroads, § 1079. Medford, etc., R. Co. v. Somerville, 111 Mass. 232. See Lake Roland R. Co. v. Mayor, 77 Md. 352, 7 Lewis Am. R. & Corp. Cas. 619, Ann.

been accepted and acted upon. It is also a grant from the state, which, when accepted by the grantee, imposes upon it the duty of serving the public which it can not lay down at will, or escape from, by merely ceasing to operate the road. It was claimed that the franchise had been abandoned, and the court said: "A mere privilege or right may, perhaps, be properly said to be abandoned in a proper case, although even in that case there must be something more than mere non-user to constitute such abandonment. * * * While a mere easement or right may be abandoned, the word is plainly inapplicable to a duty owing to the state."

In a recent Missouri case, the court, after referring to the Illinois and Michigan cases, which hold that the right to use the streets for railway tracks and gas pipes is not a state franchise, but a local easement resting on a contract, or a license, said: "But these cases we think not in line with the great weight of authority. * * * This court has recognized the rights of street railways in the streets of a municipality as franchises, and as vested rights which might be mortgaged by the company to whom the franchise belonged."[2] It was held that the privilege was a franchise and not a mere license, although granted by the municipality under legislative authority, and that *quo warranto*, in the name of the state, was the proper remedy to obtain a forfeiture for non-performance of conditions.[3]

§ 123. **The franchise of being a corporation.**—The right to be a corporation is a franchise which is necessarily granted by every charter of incorporation. When the state grants to certain persons and their successors in interest the privilege of forming a corporation and acting in a corporate capacity within certain defined limits, the privilege so granted is called the cor-

[1] Wright v. Milwaukee, etc., R. Co., 95 Wis. 29, 60 Am. St. Rep. 74. See State v. Madison, etc., R. Co., 72 Wis. 612.

[2] Hovelman v. Kansas City, etc., R Co., 79 Mo. 643.

[3] State v. East Fifth St. R. Co., 140 Mo. 539, 62 Am. St. Rep. 743.

porate franchise.[1] Under modern conditions this grant is little more than the removal of the common law prohibition, and is properly called a franchise only in the most general sense of the word.

§ 124. **In whom franchises vest.**—Some confusion exists on the question whether franchises vest in the individuals forming the corporation or in the corporation. The true rule is that the *primary* franchise of being a corporation vests in the individuals who compose the corporation and not in the corporation itself, while the *secondary* franchises, such as the right of a railway corporation to construct and operate a railway, are vested in the corporation.[2] This distinction will be clearly recognized when we come to consider the vendibility of franchises. A franchise granted by a city to an electric light company is the property of the corporation and not of the stockholders.[3] The general rule is that the primary franchise can not be sold or transferred; but the owners of a primary franchise may in effect transfer it at will, by virtue of the power they possess of naming their successors in interest. The continuity of corporate life is thus maintained, but the result is identical with that of a formal transfer of the franchise. In one instance, however, the rule is still of importance, and that is when the property and franchises of a corporation are sold under mortgage foreclosure. The purchaser at such sale may acquire the property and *secondary* franchises of the corporation, but not the primary franchise of being a corporation. Unless there is legislative authority for the transfer of the primary franchise, the purchasers must create a new corporation under the existing laws.

§ 125. **The sale and transfer of franchises.**—The rule stated in general terms is that a corporation can not, without legislative authority, mortgage, sell or transfer its franchises,

[1] Paul v. Virginia, 8 Wall. (U. S.) 181. See State v. East, etc., R. Co., 140 Mo. 539, 62 Am. St. Rep. 743, 747; N. O., etc., Co. v. Delamore, 114 U. S. 501.

[2] Fietsam v. Hay, 122 Ill. 293, 3 Am. St. Rep. 492.

[3] Payne v. Goldbach, 14 Ind. App. 100, 42 N. E. Rep. 642.

and that any attempt to do so is invalid.[1] This doctrine forbids any corporation from transferring its primary franchise of being a corporation, but under modern liberal incorporation laws it has little if any practical value. There no longer exists a reason for transferring this privilege, as it can be easily acquired by complying with the simple requirements of the statutes regulating incorporation. Franchises at common law are property rights, and subject to sale and transfer like any other property, and this restrictive rule is a limitation upon the power of the corporation and not due to the nature of the franchise. Unless the corporation is charged with some public duty, which is generally the case, no good reason exists why it should not be permitted to sell its secondary franchises.[2] The rule that the primary franchises can not be transferred is reduced to an absurdity by the simple statement that the entire personnel of the corporation may be changed in an hour by a permissible and legal transfer of all the shares of stock.

§ 126. **Corporations charged with public duties.**—The most important modern private corporations receive their franchises in consideration of the performance of some public duty. In such cases the state is supposed to impose a certain degree of confidence in the grantee, and hence insists that the duties shall be performed by the particular grantee. But here, as in all cases, a transfer may, as far as the personnel is concerned, be

[1] Thomas v. Railway Co., 101 U. S. 73; State v. Anderson, 90 Wis. 550; Middlesex, etc., R. Co. v. Boston, etc., R. Co., 115 Mass. 351; Fietsam v. Hay, 122 Ill. 293, 3 Am. St. Rep. 124; Chicago, etc., Co. v. People's, etc., Co., 121 Ill. 530, 2 Am. St. Rep. 124; Atkinson v. Marietta, etc., R. Co., 15 Ohio St. 21; Great Northern R. Co. v. Eastern, etc., R. Co., 21 L. J. Chan. 837. No implied power to mortgage franchises. Coe v. Col., etc., Co., 10 Ohio St. 372; Carpenter v. B. H., etc., Co., 65 N. Y. 43, 50. But see Kennebec, etc., R. Co. v. Portland, etc., R. Co., 59 Me. 23. The legislature may provide for the sale and transfer of all franchises created by or under its authority. State v. Anderson, 97 Wis. 114, 72 N. W. Rep. 386. A corporation which permits another company which acquires all its business to carry on the business in its name is liable for the acts of the latter. Davis, etc., Co. v. Fowler Bros., 47 N. Y. Supp. 205.

[2] State v. East, etc., R. Co., 140 Mo. 539. In N. O. R. Co. v. Delamore, 114 U. S. 501, it was held the right of way of a railway company through the streets of a city is a franchise which may be mortgaged and transferred.

made by a transfer of the stock. But the rule is settled that the corporation can sell neither the primary nor secondary franchises, which are necessary to the due and proper performance of the public duties imposed upon it by its charter. As stated by Mr. Justice Miller:[1] "Where a corporation like a railroad company has granted to it, by charter, a franchise intended in large measure to be exercised for the public good, the due performance of those duties being the consideration of the public grant, any contract which disables the corporation from performing those functions, which undertakes without the consent of the state to transfer to others the rights and powers conferred by the charter, and to relieve the grantees of the burdens which it imposes, is a violation of the contract with the state and is void as against public policy."[2]

Hence, a railway or canal company can not lease its franchises to another company or person without express legislative authority,[3] nor can a railway company by means of leases transfer its road and the use of its franchises to another company and thus exempt itself from responsibility for the management of the road.[4] In a case where this was sought to be done, the court said:[5] "Important franchises were conferred upon the corporation to enable it to provide the facilities for communication and intercourse required by the public convenience. Corporate management and control over these were prescribed, and corporate responsibility for the insufficiency provided as a remuneration to the community for their grant. The corporation can not absolve itself from the performance of its obligations, without the consent of the legislature."

[1] Thomas v. Railway Co., 101 U. S. 71, Wilgus' Cases.

[2] Gulf, etc., R. Co. v. Morris, 67 Tex. 692; Union Pac. R. Co. v. Railway Co., 163 U. S. 564; Chicago, etc., Co. v. People's, etc., Co., 121 Ill. 531; Visalia, etc., Co. v. Sims, 104 Cal. 326.

[3] Oregon R. Co. v. Railway Co., 130 U. S. 1; Van Steuben v. Centr. R. Co., 178 Pa. St. 367; Middlesex, etc., R. Co. v. Boston, etc., R. Co., 115 Mass. 347; Brunswick, etc., Co. v. United, etc., Co., 85 Me. 532; Daniels v. Hart, 118 Mass. 542.

[4] Fisher v. W. V. & P. R. Co., 39 W. Va. 366, 23 L. R. A. 758; Ricketts v. Ches., etc., R. Co., 33 W. Va. 433, 7 L. R. A. 354; Naglee v. Alexandria, etc., R. Co., 83 Va. 707.

[5] York, etc., Co. v. Winans, 17 How. (U. S.) 39.

The same principle forbids such a corporation to sell or dispose of the property which is necessary to enable it to perform its duties. It will not, however, prevent a railway company from alienating its personal property, such as its locomotive engines.[1]

§ 127. **Transfer under legislative authority — Construction.**—The legislature may authorize a corporation to transfer either its primary or its secondary franchises.[2] A law authorizing a corporation to transfer its franchises does not necessarily deprive it of its own franchises. The transferee may merely acquire a new franchise by appointment of the legislature. It is for the legislature to say whether or not the franchise of the old company is extinct.[3] Authority to transfer a "charter" or "the franchise to be a corporation," authorizes the grantee to confer the right to form a corporation upon such persons as he shall indicate by deed, or as shall become the purchasers at foreclosure sale. As said by Chief Justice Welch,[4] "The real transaction in all such cases of transfer, sale, or conveyance, in legal effect is nothing more or less, and nothing other, than a surrender or abandonment of the old charter by the corporators, and a grant *de novo* of a similar charter to the so-called transferees or purchasers. To look upon it in any other light, and to regard the transaction as a literal transfer or sale of the charter, is to be deceived, we think, by a mere figure of speech. The vital part of the transaction, and that without which it would be a nullity, is the law under which the transfer is made. The statute authorizing the transfer and declaring its effect, is the grant of a new charter, couched in few words, and to take effect upon condition of the surrender or abandonment of the old charter; and the deed of the transfer is to be regarded as mere evidence of the surrender or abandonment."

[1] Coe v. Col., etc., R. Co., 10 Ohio St. 372, 75 Am. Dec. 518.

[2] Chapman, etc., Co. v. Oconto, etc., Co., 89 Wis. 264, 46 Am. St. Rep. 830. See monographic note to Brunswick, etc., Co. v. United, etc., Co., 35 Am. St. Rep. 390, 396.

[3] See Morawetz Priv. Corp., § 936.

[4] State v. Sherman, 22 Ohio St. 411 Quoted in Memphis, etc., R. Co. v. Railroad Com'rs, 112 U. S. 609.

Power to sell or mortgage the franchise of being a corporation is never implied from authority to sell or mortgage "the property and franchises" of a corporation.[1] It is not essential in such case that the purchaser should be a corporation, in order to acquire the property and secondary franchises. Where the question was under discussion, Mr. Justice Matthews said:[2] "The franchise of being a corporation need not be implied as necessary to secure the mortgage bondholders, or the purchasers at a foreclosure sale, the substantial rights intended to be secured. They acquire the ownership of the railroad and the property incident to it, and the franchise of maintaining and operating it as such, and the corporate existence is not essential to its use and enjoyment. All the franchises necessary or important to the beneficial use of the railroad could as well be exercised by natural persons."

A provision in the charter to the effect that the purchasers at a foreclosure sale may organize as a corporation will be construed as conferring only the right to organize according to such laws as are in force at the time when the organization takes place.[3] Authority to a railroad corporation to mortgage its "road, income and property," does not authorize a mortgage of its franchises.[4]

§ 128. **Franchises pertaining to use of particular property.**—Authority to sell and transfer certain particular property authorizes the transfer to the purchaser of all franchises which pertain to the use of that property.[5] But only such

[1] Coe v. Col., etc., R. Co., 10 Ohio St. 372; Eldridge v. Smith, 34 Vt. 484. Compare Pierce v. Emery, 32 N. H. 484, St. P., etc., R. Co. v. Parcher, 14 Minn. 297; Cook v. Detroit, etc., R. Co., 43 Mich. 349.

[2] Memphis, etc., R. Co. v. Railroad Co., 112 U. S. 609.

[3] Memphis, etc., R. Co. v. Railroad Co., 112 U. S. 609.

[4] Pullan v. Cincinnati, etc., R. Co., 4 Bissell 35.

[5] New Orleans, etc., Co. v. Delamore, 114 U. S. 501; Branch v. Jessup, 106 U. S. 468; Pierce v. Milwaukee, etc., R.Co., 24 Wis. 551. "It is immaterial whether the right of using and operating the railroad be regarded as a statutory right called a franchise, or as a license conferred by a municipality, or as a mere easement or property right conferred under the common law; a transfer of the property pursuant to authority conferred by law

franchises as are *necessary* to the enjoyment of the property transferred pass with it to the grantee. Hence, a lease of a railroad company's property does not confer upon the lessee the right to exercise the power of eminent domain, although it is necessary in order to complete the line and the power was possessed by the lessor.[1] But express authority to transfer the "property and franchises" authorizes the company to sell the franchises which are *incidental* as well as those which are *necessary* to the enjoyment of the property. Under such authority the transferee would acquire the right of eminent domain when necessary to complete the construction of the railway line purchased.[2] The distinction between franchises which are necessary to the use of particular property and those which are not is well illustrated by the case of an exemption from taxation. Such unusual privileges are not necessary to enable the transferee to use and maintain the property, and hence do not pass to the purchaser. The immunity from taxation in such cases is not strictly a franchise but a personal privilege of the company, and is not transferrable. Hence upon a sale of the property and franchises of a railway corporation under a decree founded upon a mortgage which in terms covers the franchises, or under a process upon a money judgment against the company, immunity from taxation upon the property of the company provided in the act of incorporation does not accompany the property in its transfer to the purchaser.[3] So where the law provides that the purchasers under a foreclosure sale of a railroad shall "succeed to all such franchises, rights and privileges * * as would have been had * * by the first company but for such sale and conveyance" the purchaser does not acquire exemption from taxation. Such exemption is personal to the company and does not inhere in the property.[4]

would include a transfer of every right necessary for its continued operation." Morawetz Priv. Corp., § 932.

[1] Mayor, etc., v. Norwich, etc., Co., 109 Mass. 103.

[2] North Carolina, etc., Co. v. Carolina, etc., R. Co., 83 N. C. 489.

[3] Morgan v. Louisiana, 93 U. S. 217; Memphis, etc., R. Co. v. Railway Comrs., 112 U. S. 609. See § 119*a*, *supra*.

[4] Chesapeake, etc., R. Co. v. Miller, 114 U. S. 176.

Where a ferry is practically an extension of a railroad, the ferry franchise passes with the sale of the railroad without special mention.[1]

§ 129. **Forfeiture of franchises.**—From the nature of a franchise it logically follows that only the state can question the right to its enjoyment, and begin proceedings to forfeit such a right for non-user or misuser.[2] A total non-user of a franchise may exist for so long a time and under such circumstances that a surrender of the franchise by the corporation, and acceptance of such surrender on the part of the state, will be presumed.[3] There appears to be but one exception to the rule that the forfeiture of a franchise must be declared in a direct proceeding by the state. When the franchise is granted upon an express condition which is to be performed within a certain time, as the construction of a line of railway to a certain place within a certain specified time, the forfeiture takes place *ipso facto* upon failure to perform the condition; and the failure may be ascertained in any proper collateral proceeding.[4]

§ 130. **Constitutional protection of franchises.**—It is the settled rule of American constitutional law that "whenever the sovereign power for the time being within its legitimate sphere of action—whether it be the king in his council, as in colonial times, or the congress of the United States, or the legislature of a state, or the council of a municipal corporation acting under the authority derived from the constitution or statute law of the state within which it exists—grants to a body of co-adventurers the franchise of being a corporation, or any

[1] Brownell v. Old Colony R. Co., 164 Mass. 29, 29 L. R. A. 169.

[2] Elizabeth, etc., Co. v. Green, 46 N. J.Eq. 118, 18 Atl. Rep. 844; Combes v. Keyes, 89 Wis. 297, 46 Am. St. Rep. 839; Attorney-General v. Superior, etc., R. Co., 93 Wis. 604.

[3] Combes v. Keyes, 89 Wis. 297, 46 Am. St. Rep. 839, and cases cited; Wright v. Milwaukee, etc., R. Co., 95 Wis. 29. That a corporation may forfeit its franchise by non-user or misuser, see note to Atchison, etc., R. Co. v. Nave, 5 Am. St. Rep. 804.

[4] Oakland R. Co. v. Oakland, etc., R. Co., 45 Cal. 365, 13 Am. Rep. 181; Belleville v. Cit., etc., R. Co. 152 Ill., 171, 26 L. R. A. 681. Compare Willamet & Co. v. Kittridge, 5 Saw.(U.S.) 44.

other species of franchise, privilege, or license in the nature of property, and the grantees accept the grant—such franchise, privilege or license, is within the constitutional protection in such a sense that it can not thereafter be revoked or repealed by any form of state action against the consent of the corporation, although it may be seized by the state for misuser or nonuser.''[1] This general rule is subject to the qualifications that the state may reserve to itself at the time of making the grant the right to repeal or alter the grant, to a reasonable exercise of the police power, and the power of eminent domain. No rights, however, attach until after acceptance of the grant.[2]

[1] Thompson Priv. Corps., §§ 5381–2. This doctrine rests on the famous case of Dartmouth College v. Woodward, 4 Wheat. (U. S.) 518, and the long line of authorities with which that case has been followed. That corporations are entitled to protection in their rights as owners of property, see St. Louis, etc., R. Co. v. Paul, 64 Ark. 83, 62 Am. St. Rep. 168, and cases cited in note.

[2] In Illinois, etc., R. Co. v. Illinois, 146 U. S. 387, it was held that there can be no irrepealable contract in a conveyance of property by a grantor in disregard of a public trust under which he was bound to hold and manage it.

CHAPTER 6.

POWERS.

§ 131. General statement.

I. The Theory of Corporate Power.

132. The theory of general capacity.
133. The theory of special capacities.
134. Principles of construction.
135. Presumption of power and regularity.
136. Place where powers may be exercised.
§ 137. Grant of power—Not limited by term of corporate existence.

II. Classification of Powers.

138. Express powers.
139. Powers implied from express powers.
140. Incidental powers.

§ 131. **General statement.**—Power in a legal sense signifies legal competence, capacity or right.[1] A corporation created by the sovereign power for particular purposes has such powers only as the state grants to it. Unlike a natural person, it does not possess those general powers which are common to all. The general scope of corporate power is ordinarily determined by a consideration of the purpose for which the corporation was organized. The mere fact of creation implies a grant of those powers which are essential to corporate existence. The state may, in the charter, enumerate specific powers granted, or it may grant authority to do a certain thing, in general terms. In the latter case the power to do all things proper and necessary in order to carry out the purpose of the corporate creation is implied. Thus a trading or manufacturing corporation has the same authority as an individual trader or manufacturer as to the manner of selling goods, selecting selling agents, and imposing conditions as to terms of sales.[2] The legislatures and courts have proceeded upon two theories in determining

[1] See Bissell v. Michigan, etc., R. Co., 22 N. Y. 258, 264.

[2] Stockton v. American, etc., Co., N. J. Ch., 36 Atl. Rep. 971.

corporate powers; viz., the theory of general corporate capacity, and the theory of special capacities.

I. The Theory of Corporate Power.

§ 132. **The theory of general capacity.**—The theory of the general capacity of corporations is recognized by the English authorities. It is probable that this is the theory of the common law, and that the theory of special corporate capacities which is now the established rule of the American courts is a departure. According to this doctrine, as stated by Sir Frederick Pollock,[1] "a corporation once duly constituted has all such powers and capacities of a natural person as in the nature of things can be exercised by an artificial person. Transactions entered into with apparent authority in the name of the corporation are presumably valid and binding, and are invalid only if it can be shown that the legislature has expressly or by necessary implication deprived the corporation of the power it naturally would have had of entering into them. The question is, therefore, was the corporation forbidden to bind itself by this transaction." This rule, however, is subject to the important qualification established by the leading case of Ashbury Railway Company v. Riche,[2] that "where there is an act of parliament creating a corporation for a particular purpose, and giving it powers for that particular purpose, what it does not expressly or impliedly authorize is to be taken as prohibited.[3]

[1] Pollock on Contracts, page 119, and see Appendix, note D, "Limits of Corporate Power."

"The English have been unwilling to grant in terms the privilege of complete incorporations, as of right, to all who desire it, because in their law it has been regarded as an essential attribute of a full corporation; first, that its personality is wholly distinct from that of its members; second, that therefore they can not, in fairness, be made liable for its obligations individually; and, third, that it can exercise every power not prohibited by its charter. Coke had laid the foundations of this doctrine in discussing the attributes of an incorporated hospital, and it has been silently extended in course of time to corporations of every class." Baldwin Modern Pol. Inst., page 206.

[2] L. R. 7 H. L. 653.

[3] Attorney-General v. Great Eastern R. Co., 5 App. Cas. 481.

The effect of this exception is to very materially modify the general rule. "The rule of law is," says Mr. Justice Blackburn, "that a corporation at common law has, as an incident given by law, the same power to contract and is subject to the same restrictions as a natural person. And this is important when we come to construe the statutes creating a corporation, for, if it were true that a corporation at common law has a capacity to contract to the extent given it by the instrument creating it, and no further, the question would be, does the statute creating the corporation, by express provision or necessary implication, show an intention in the legislature to confer upon the corporation capacity to make the contract? But if a body corporate has, as incident to it, a general capacity to contract, the question is, does the statute creating the corporation, by express provision or necessary implication, show an intention in the legislature to prohibit and so avoid the making of the contract of this particular kind?"

§ 133. **The theory of special capacities.**—The American courts have adopted what is known as the "Doctrine of Special Capacities" in dealing with questions of corporate power. This was also the doctrine of the earlier English cases which adopted it from the equity decisions where for particular reasons it was long maintained. It is also apparent that the draughtsmen of the English statutes proceeded upon this theory, as they attempted to enumerate the specific powers granted instead of enumerating restrictions. Taken, however, in connection with the limitations imposed upon the general rule as stated in the preceding section, there is very little practical difference between the two doctrines. It matters little which we adopt for the purpose of determining whether a given act of a particular corporation is *ultra vires*. It is very important, however, when we are to determine the effect to be given an unauthorized contract of a corporation. Under one theory the act rests upon a want of capacity, and under the other it is an act expressly forbidden. The rule of general capacity was strenuously con-

tended for in the well-known case of Thomas v. Railroad,[1] but the court gave its adherence to the doctrine of special capacity and stated the rule in the following language: "We take the general doctrine to be, in this country, although there may be exceptional cases and some authorities to the contrary, that the powers of corporations organized under legislative statutes are such, and such only, as those statutes confer. Conceding the rule applicable to all statutes, that what is fairly implied is as much granted as what is expressed, it remains that the charter of a corporation is the measure of its powers, and that the enumeration of these powers implies the exclusion of all others."

§ 134. **Principles of construction.**—The controlling rule for the construction of corporate charters is stated by Mr. Justice Miller, in the language quoted in the preceding section. The charter of the corporation, read in connection with the

[1] Thomas v. Railway Co., 101 U. S. 82; State v. Lincoln, etc., Co. (Mo.), 46 S. W. Rep. 593. The rule is thus stated in a recent case: A corporation is a mere creation of law, and has only such powers as are expressly granted by the state as are necessary to carry into effect the powers expressly granted. Wyeth, etc., Co. v. James-Spencer Bateman, etc., Co. (Utah), 47 Pac. Rep. 604. The cases supporting this statement are so numerous as to make citation almost unnecessary. See Valley R. Co. v. Lake Erie, etc., Co., 46 Ohio St. 50; Humbolt, etc., Co. v. American, etc., Co., 62 Fed. Rep. 361; Straus v. Insurance Co., 5 Ohio St. 60. This doctrine is criticised in a recent magazine article, in which the position of the supreme court of the United States is examined. It is said: "It is obviously logical to refuse to enforce an agreement if one or both of the parties lacks the necessary contractual capacity, but does not the inconvenience of the conclusion call for a re-examination of the premise? It is submitted that we shall never see our commercial law in a satisfactory state until the courts re-establish the common law doctrine of general capacities, treating contracts made beyond the limits of chartered activity as contracts prohibited but not void, and leaving the state to punish the disregard of the prohibition while enforcing the contract between the parties. The enforcement of corporate contracts, in spite of objections to the corporate power, represents the overwhelming tendency of American decisions. The supreme court has given the contrary doctrine a fair trial and the result is, from a practical point of view, a failure." Unauthorized Corporate Contracts, a comment on Pullman Palace Car Co. v. Central Transportation Co., 171 U. S. 138, by George Wharton Pepper, Yale Law Journal, vol. 8, 1898.

general laws applicable to it, is the measure of the powers of the corporation, and any contract in excess of such powers will not be sustained. But it is equally true that whatever, under this charter and general laws, reasonably construed, may be regarded as incidental to the objects for which the corporation was created, is not to be taken as prohibited. It is often said that corporate charters should be strictly construed against the corporation, but this should be treated as an exception to the general rule.[1] While nothing is to be taken as granted which is not fairly expressed or implied in the charter, the language of the charter should be given a fair construction. From the language of some of the decisions it might be thought that it is the duty of courts to make every effort to find a means to defeat the apparent language of the charter. The intent of the legislature must govern, and if it appears by a fair and reasonable construction of the language of the charter that that intent was to grant the power, it must be given effect. Certain general principles of construction are applicable to grants to corporations as well as to natural persons. Thus, grants of exclusive privileges,[2] or of powers in derogation of public right,[3] or whereby the state restricts its own action,[4] are to be construed strictly against the grantee and in favor of the public. Nothing passes by implication. But, as said by Chief Justice Bigelow:[5] "We know of no rule or principle by which an act creating a corporation for certain specific objects, or to carry on a particular trade or business, is to be strictly construed as prohibitory of all

[1] Pearsall v. Great Northern R. Co., 161 U. S. 646; Parker v. Railway Co., 7 Man. & G. 288; State v. Payne, 129 Mo. 468; Black v. Canal Co., 24 N. J. Eq. 474; Fertilizer Co. v. Hyde Park, 97 U. S. 659; First M. E. Church v. Dixon (Ill.), 52 N. E. Rep. 891; People v. Pullman, etc., Co., 175 Ill. 125.

[2] Richmond, etc., R. Co., v. Railroad Co., 13 How. (U. S.) 71; Charles River, etc., Co. v. Warren Bridge, 11 Pet. (U. S.) 420; Indianapolis, etc., Co. v. Citizens', etc., Co., 127 Ind. 369.

[3] Downing v. Mt. Wash. R. Co., 40 N. H. 230; Fertilizing Co. v. Hyde Park, 97 U. S. 659; Providence Bank v. Billings, 4 Pet. (U. S.) 514.

[4] As an exemption from taxation, Wilmington, etc., R. Co. v. Alsbrook, 146 U. S. 279; Railroad Co. v. Gaines, 97 U. S. 697.

[5] Brown v. Winnisimmet Co., 11 Allen (Mass.) 326.

other dealings or transactions not coming within the exact scope of those designated. Undoubtedly the main business of a corporation is to be confined to that class of operations which properly appertain to the general purposes for which its charter was granted. But it may also enter into contracts and engage in transactions which are incidental or auxiliary to its main business, or which may become necessary, expedient, or profitable in the care and management of the property which it is authorized to hold under the act by which it was created." An enumeration of powers as granted by implication excludes all others not necessary or proper to carry those enumerations into effect.[1]

§ 135. **Presumption of power and regularity.**—Persons dealing with a corporation are entitled to assume that it is acting within the scope of its powers and is observing all the requirements with reference to the manner of exercising its power. If the act appears to be within the charter powers, the public, in the absence of notice to the contrary, has the conclusive right to presume that the act is valid.[2] Thus, a mortgagee dealing in good faith with a corporation may assume that provisions or regulations contained in the by-laws have been complied with.[3]

§ 136. **Place where powers may be exercised.**—A corporation has implied authority to exercise its powers beyond the jurisdiction of the state by which it is created, subject, however, to limitations imposed by the foreign state. In order to comply with conditions so imposed, a corporation may deposit security with an officer of the foreign state, as required by its statute.[4] If the charter requires the business to be carried on in a certain place, the corporation can not locate at a different place, but when no place is designated it may be at any place in the state.[5]

[1] Case v. Kelly, 133 U. S. 21; Farmers', etc., Bank v. Baldwin, 23 Minn. 198; Life, etc., Co. v. Mech., etc., Co., 7 Wend. (N. Y.) 31.

[2] Louisville, etc., Co. v. Louisville, etc., R. Co., 75 Fed. Rep. 433, 43 U. S. App. 550.

[3] Ashley, etc., Co. v. Illinois, etc., Co., 164 Ill. 149, 45 N. E. Rep. 410.

[4] Lewis v. American, etc., Assn. (Wis.), 73 N. W. Rep. 793, 39 L. R. A. 559.

[5] Stickle v. Liberty, etc., Co. (N. J.), 32 Atl. Rep. 708.

137. **Grant of power—Not limited by term of corporate existence.**—A limitation on the term of the corporate existence common under modern statutes does not prevent the corporation from taking a grant of power or a franchise to itself and assigns, absolute in terms and without limitation as to time of enjoyment. Thus a street railway company, having a corporate existence of thirty years, may take a grant of the privilege of operating its road for a longer period.[1] On the same principle, a corporation may take a fee-simple estate in real estate and may transfer the same absolutely, and its title is not affected by the subsequent dissolution of the corporation.[2] "The fact that it can not personally enjoy the interest thus granted after the expiration of its substantial and corporate franchises, would not cut down the estate granted. Its power of alienation was unaffected, and its assignee, if otherwise endowed with the franchises essential to the operation of street railways, might enjoy the rights and privileges derived by assignment."[3]

A right of way obtained by condemnation is not limited to the period of the charter of the original corporation; it passes to its successor under a consolidation act, and, having been taken for railroad uses, remains for such during the extended period.[4]

II. Classification of Powers.

§ 138. **Express powers.**—Where corporations are organized under special charters, there can be but little difficulty in determining what powers are expressly granted. Under general incorporation laws, the articles of incorporation are in effect special charters which must be read and construed in connection with the general laws of the state. When the statute or charter specifically enumerates the powers which corporations

[1] Detroit, etc., Ry. Co. v. Detroit, 64 Fed. Rep. 628, 26 L. R. A. 667; Omaha Bridge Cases, 51 Fed. Rep. 309, 2d C. C. A. 174; People v. O'Brien, 111 N. Y. 1, 2 L. R. A. 255.

[2] 2 Kent's Com. 281. See cases cited in § 167, *infra*.

[3] Detroit, etc., R. Co. v. Detroit, 64 Fed. Rep. 628, 26 L. R. A. 667.

[4] Davis v. Memphis, etc., R. Co., 87 Ala. 633. Same principle, see Bass v. R. N., etc., Co., 111 N. C. 439, 16 S. E. Rep. 402.

organized thereunder shall possess, it impliedly limits the powers to such as are thus enumerated. A general statute of this character authorizing the organization of corporations with certain powers only, the mere claim of other powers made in the articles of incorporation is of no effect.[1]

§ 139. **Powers implied from express powers.**—A power specifically granted carries with it by implication such other powers as are reasonably necessary to carry the powers expressly granted into execution. "An incidental power is one that is directly and immediately appropriate to the execution of the specific power granted, and not one which has a slight or remote relation to it."[2] In order to derive a power by implication, it must appear that such power is necessary to the enjoyment of the specially granted right, without which the latter would fail.[3] Necessary, in this sense, does not mean indispensable; it means suitable and proper to accomplish the end which the legislature had in view at the time of the grant of the charter.[4] A very liberal construction will be given to charters of corporations formed for the purpose of promoting public improvements.[5] The courts will not investigate the expedience of their action or inquire whether or not other and better means might have been adopted for the purpose of accomplishing the desired objects.[6] Within the scope of their

[1] Oregon, etc., R. Co. v. Oregonian R. Co., 130 U. S. 1; Thomas v. Railway Co., 101 U. S. 71; Wyeth, etc., Co. v. James-Spencer Bateman Co. (Utah), 47 Pac. Rep. 607

[2] People v. Chicago, etc., Co., 130 Ill. 268; Franklin County v. Lewiston, etc., 68 Me. 43.

[3] Downing v. Mt. Washington R. Co., 40 N. H. 230.

[4] State v. Hancock, 35 N. J. L. 537. See State v. Pullman, etc., Co., 175 Ill. 125, and authorities cited in dissenting opinion, p. 167.

[5] Taggart v. Newport, etc., R. Co., 16 R. I. 668, 19 Atl. Rep. 326.

[6] Oglesby v. Attrill, 105 U. S. 605. In Curtis v. Leavitt, 15 N. Y. 9, Comstock, J., said: "It is plain that corporations executing their expressed powers are not confined to means of such indispensable necessity that without them there could be no execution at all. The contrary doctrine would lead at once to a very great absurdity; for, if there are several modes of accomplishing the end, neither one is indispensable, and each would exclude all the others. And thus, by inevitable logic, an expressed grant of power would be forever dormant, because there are more modes

authority corporations have all the powers of natural persons, and having the power to engage in a certain business, they may adopt such means and carry on the business in the manner in which that kind of business is usually carried on.[1] The charter of a corporation need not be consulted for authority to make contracts and to sell and mortgage its property. It may exercise its common law right in these matters like an individual.[2]

But a small proportion of the powers actually exercised by private corporations are granted to them in express terms by the general law or by their charter. When so granted, the question of authority can not arise, and as a consequence questions of corporate power ordinarily arise when it is sought to exercise a power as implied from an express power.

A corporation can not engage in a business different from that authorized by its charter,[3] but this rule does not prevent it from carrying on a business which is incidental to the principal business. Thus a manufacturing corporation may, under certain conditions, run a supply store;[4] a railway company a restaurant,[5] or a mining company a transportation company, when necessary for carrying its products to market.[6] But a manufacturing corporation has no implied power, under a charter provision giving it authority to acquire and

than one of carrying it into execution." See Ellerman v. Chicago, etc., R.Co., 49 N. J. Eq. 217, 23 Atl. Rep. 287.

[1] Deringer v. Deringer, 5 Houston (Del.) 416, 1 Am. St. Rep 150.

[2] White Valley, etc., Co. v. Vallette, 21 Howard (U. S.) 414; Wright v. Hughes, 119 Ind. 324; Commissioners v. Atlantic, etc., R. Co., 77 N. C. 289; Lehigh Valley, etc., Co. v. West, 63 Wis. 45.

[3] People v. Campbell, 144 N. Y. 166; Chewacla Lime Works v. Dismukes, 87 Ala. 344; Weckler v. Hagerstown Nat'l Bank, 42 Md. 581, 20 Am. Rep. 95; Rochester Ins. Co. v. Martin, 13 Minn. 59; Miller v. Insurance Co., 92 Tenn. 167.

[4] Seabright v. Payne, 6 Lea (Tenn.) 283; Dauchy v. Brown, 24 Vt. 197. A brewing company may run a saloon. Welsh v. Heim Brew. Co., 47 Mo. App. 608. A gas company may deal in patent appliances and conveniences which have a tendency to increase sales of gas. Malone v. Lancaster Gas Co., 182 Pa. St. 309.

[5] Jacksonville, etc., R. Co. v. Hooper, 160 U. S. 514; Flanagan v. Great Western R. Co., L. R. 7 Eq. 116; Texas, etc., R. Co. v. Robards, 60 Tex. 545 (hotel).

[6] Moss v. Averell, 10 N. Y. 449; Callaway, etc., Co. v. Clark, 32 Mo. 305.

hold such real estate as may be deemed necessary for the successful prosecution of its business, to purchase near a populous city several hundred acres of open prairie as a site for its plant and subdivide the land not occupied by the plant into lots and blocks, with streets, alleys and parks, erect houses, churches, school buildings, stores, and rent them to employes, religious denominations, school boards and business men; nor can such action be sustained on the ground of expediency, or of necessity in providing its employes with shelter, educational advantages, markets, and places of worship and amusement. These enterprises were not necessary to the successful carrying out of the purposes of the corporation, and should have been left to private capital and enterprise.[1]

§ 140. **Incidental powers.**—The old books enumerate five powers which are said to be necessarily and inseparably incident to every corporation. As soon as a corporation is duly created, it has as incidental to its existence the right:

(1) To have perpetual succession.

(2) To sue or be sued, to implead or be impleaded, grant or receive by its corporate name, and do all other acts that natural persons may.

(3) To purchase lands and hold them for the benefit of themselves and their successors.

(4) To have a common seal.

(5) To make by-laws or private statutes for the better government of the corporation.[2]

"These *indicia*," said Chief Justice Nelson,[3] "were given by judges and elementary writers at a very early day; since which time the institutions have greatly multiplied, their practical operation and use have been very thoroughly tested, and their peculiar and essential properties much better understood. Any one comprehending the scope and purpose of them at this day,

[1] People v. Pullman, etc., Co., 175 Ill. 125, three judges dissenting. The dissenting opinion contains an elaborate discussion of the authorities on the doctrine of implied power.

[2] 1 Black. Com., p. 416; Case of Sutton's Hospital, 10 Rep. 30.

[3] Thomas v. Dakin, 22 Wend. (N. Y.) 9, Wilgus' Cases.

will not fail to perceive that some of the powers above specified are of trifling importance while others are wholly unessential. For instance, the power to purchase and hold real estate is not otherwise essential than to afford a place of business, and the right to use a common seal or to make by-laws may be dispensed with altogether. For, as to the one, it is now well settled that corporations may contract by resolution or through agents without seal; and as to the other, the power is unnecessary in all cases where the charter sufficiently provides for the government of the body. The distinguishing feature far above all others is in the capacity conferred, by which a perpetual succession of different persons shall be regarded in the law as one and the same body, and may at all times act in fulfillment of the objects of the association as a single individual. In this way a legal existence, a body corporate, an artificial being is constituted, the creation of which enables any number of persons to be concerned in accomplishing a particular object as one man. While the aggregate means and influence of all are wielded in effecting it, the operation is conducted with the simplicity and individuality of a natural person. In this consists the essence and great value of these institutions. Hence it is apparent that the only properties that can be regarded strictly as essential are those which are indispensable to mould the different persons into this artificial being and thereby enable it to act in the way above stated. When once constituted, this legal being created, the powers and faculties that may be conferred are various—limited or enlarged at the discretion of the legislature, and will depend upon the nature and object of the institution, which is as competent as a natural person to receive and enjoy them. We may, in short, conclude by saying with the most approved authorities at this day, that the essence of corporation consists in a capacity:

"(1) To have a perpetual succession under a special name and in an artificial form.

"(2) To take and grant property, contract obligations, sue and be sued by its corporate name as an individual, and

"(3) To receive and enjoy in common grants of privileges and immunities."

CHAPTER 7.

POWERS INCIDENTAL TO CORPORATE EXISTENCE.

§ 141. In general.
142. Perpetual succession.
143. To have a seal.

I. By-Laws.

144. Definition.
145. Power to make by-laws.
146. In whom vested.
147. Manner of adoption.
148. General requirements — Must conform to charter.
149. Must not be repugnant to law of the land.
150. Public policy.
151. Must be reasonable.
152. Must be general.
153. Effect of by-laws—As to members and officers.
154. Effect upon third persons.
155. By-laws limiting powers of agents.
§ 156. Rules and regulations published by corporations.
157. By-laws imposing forfeiture.
158. Expulsion of members.
159. Amendment, repeal and waiver.

II. Power to Take and Hold Land.

160. The common law rule.
161. Statutory restrictions.
162. Distinction between power to take and to hold.
163. Manner of acquiring title.
164. Power to take by devise.
165. Devise to corporation—Statutory limit.
166. The doctrine of equitable conversion.
167. The estate which may be taken.
168. Who can question the right of the corporation.

§ 141. **In general.**—As stated in the preceding section, certain powers are possessed by every corporation as incidental to its existence as a corporation. They are implied from the fact of the existence of the corporation. In many cases the same powers are specifically granted in the charter or general incorporation statute.

§ 142. **Perpetual succession.**—It is said to be of the very essence of a common law corporation that it have perpetual succession, and, therefore, as Blackstone says, "all corporations have a power necessarily implied of electing members in the room of such as go off."[1] In modern times, however,

[1] 1 Black. Com., p. 474.

perpetual succession means nothing more than the continuity of the corporate life during the period prescribed for the corporate existence. Although the personnel may change, the corporation retains its identity. The words "perpetual succession" in the charter of a corporation formed by purchasers under a deed of trust of the property of a prior corporation whose term of life was thirty years, mean nothing more than a continuous succession during the existence of the corporation for the limited period.[1] After the decision in the Dartmouth College case, it became the practice to limit the life of a corporation to a certain period in order that the state might retain proper control over it.[2]

§ 143. **To have a seal.**—Whether corporation seals originated like private seals, in general ignorance, or in the peculiar nature of corporations aggregate,[3] it became in the course of time a power incidental to every corporation aggregate to have a common seal. The common law rule was that a corporation spoke through its seal.[4] The modern rule is that in the absence of a statute requiring a seal, a corporation may make a binding contract without a seal when an individual may do so.[5]

I. By-Laws.

§ 144. **Definition.**—A by-law is a rule of permanent character adopted by a corporation for the regulation of its internal

[1] State v. Hannibal, etc., R. Co., 138 Mo. 332; 39 S. W. Rep. 910. But the existence of a corporation is not limited to the unexpired term of its predecessor, which was organized under a law limiting its existence to thirty years, when the new charter confers all the rights and privileges that would have been had if the company had been organized under such statute.

[2] See note to Tussaud v. Tussaud, L. R. 44 Ch. Div. 678, in 32 Am. and Eng. C. C. 11.

[3] 1 Black. Com., p. 475.

[4] Case of Sutton's Hospital, 10 Rep. 30*b*, 7 Eng. Rul. Cas. 233, note. The corporate seal is prima facie evidence of the fact that it was fixed by proper authority. Morris v. Keil, 20 Minn. 531; Indianapolis R. Co. v. Morganstern, 103 Ill. 149.

[5] Crawford v. Longstreet, 43 N. J. L. 325; Muscatine, etc., Co. v. Muscatine, etc., Co., 85 Iowa 112; Thomas v. Dakin, 22 Wend. (N. Y.) 9. A seal is not necessary on a stock certificate. Halstead v. Dodge, 19 J. & S. (N. Y.) 169.

government. The office of a by-law is to regulate the conduct and define the duties of the members toward the corporation and between themselves.[1]

§ 145. **Power to make by-laws.**—This is one of the powers implied in the grant of the franchise of being a corporation. "It is implied in the charter of every private corporation formed for the pecuniary profit of its members, that the majority shall have power to make reasonable rules and regulations, or by-laws, for the better government of the company."[2] But the right is now generally granted in express terms. Thus, the statute of Minnesota provides that all corporations shall have power "to make by-laws and regulations consistent with the laws of the state, for their own government, and for the due and orderly conduct of their affairs, and the management of their property."[3] In certain kinds of corporations, such as

[1] Flint v. Pierce, 99 Mass. 68. Distinction between a resolution and a by-law, see Drake v. Hudson, etc., R. Co., 7 Barb. 508. A court will not take judicial notice of a by-law. Haven v. Asylum, 13 N. H. 532.

[2] Engelhardt v. Fifth Ward, etc., Assn., 148 N. Y. 281, 35 L. R. A. 289; Case of Sutton's Hospital, 10 Rep. 23*a*; Martin v. Nashville, etc., Assn., 2 Coldw. (Tenn.) 418; People v. Crossley, 69 Ill. 195; Kearney v. Andrews, 10 N. J. Eq. 70; Juker v. Comw., 20 Pa. St. 484. "That every by-law by which the benefit of the corporation is advanced is a good by-law, for that very reason, that being the true touchstone of all by-laws." Carth. 482, *per* Lord Holt. A provision of the charter of a new benevolent association binding the new association to pay all the liabilities of the old association, which has been dissolved by the expiration of the period of limitation fixed by its charter, does not of itself revive the old corporation, or give any life to by-laws attempted to be adopted by it after its legal dissolution. Supreme Lodge v. Weller (Va.), 25 S. E. Rep. 891.

[3] Gen. Stat. Minn., 1878, vol. 2, p. 392. A corporation may usually, by its by-laws, where no other provision is specially made, provide for: 1. The time, place and manner of calling and conducting its meetings. 2. The number of stockholders or members constituting a quorum. 3. The mode of voting by proxy. 4. The time of the annual election for directors and the mode and manner of giving notice thereof. 5. The compensation and duties of officers. 6. The manner of election and the tenure of office of all officers other than the directors; and 7. Suitable penalties for violation of by-laws, fixed at any reasonable amount, in no case to exceed the statutory minimum. In an early case, Norris v. Stops, Hobart, 211*a* (1614–1625), it was said: "Now, I am of opinion that, though power to make laws is given by special clause in all incorporations, yet it is needless; for I hold it to be included, by law, in the very act of incorporating, as is also the

clubs, and chambers of commerce, and boards of trade, extensive power is given to make rules to govern the conduct of the members. Such a corporation, if authorized by statute or charter, may by by-law provide for the expulsion of a member for a dishonorable act, and may provide that his membership can not be sold or transferred so long as he is indebted to any other member.[1]

§ 146. **In whom vested.**—In the absence of a charter provision to the contrary the power to make by-laws is vested in the members at large,[2] but it may be granted to the board of directors by the charter or general law, or delegated to it by the stockholders,[3] in which case the right is impliedly taken away from the body at large.[4] But under general authority to pass by-laws the board of directors can not alter a by-law which was adopted by the stockholders as a limitation upon the power of the directors.[5]

§ 147. **Manner of adoption.**—By-laws may be adopted without the use of the corporate seal, and no writing is necessary. Their existence may be established by custom or by the acquiescence of those authorized to make them.[6] But statutory formalities, modes and limitations with reference to the adoption of by-laws must be strictly observed.[7]

§ 148. **General requirements—Must conform to charter.**—There are certain general principles which must govern in the

power to sue, to purchase, and the like."

[1] Green v. Board of Trade, 174 Ill. 585, 51 N. E. Rep. 599; In re Haebler (N. Y.), 44 N. E. Rep. 87; Comw. v. Union League, 135 Pa. St. 301; Hyde v. Woods, 94 U. S. 523. See § 158.

[2] Morton, etc., Co. v. Wysong, 51 Ind. 4; People v. Crossley, 69 Ill. 195; Carroll v. Mullanphy, etc., 8 Mo. App. 249; Rex v. Westwood, 2 Dow & C. 21.

[3] Heintzelman v. Druids, etc., Assn., 38 Minn. 138; Stevens v. Davidson, 18 Gratt. (Va.) 819; Cahill v. Insurance Co., 2 Doug. (Mich.) 123; Rex v. Spencer, 3 Burr 1827.

[4] King v. Westwood, 4 Barn. & C. 798. See People v. Sterling, etc., Co., 82 Ill. 457; Calder, etc., Co. v. Pilling, 14 M. & W. 81.

[5] Stevens v. Davidson, 18 Gratt. (Va.) 819.

[6] State v. Curtis, 9 Nev. 335; Henry v. Jackson, 37 Vt. 431; Morrison v. Dorsey, 48 Md. 462; Union Bank v. Ridgely, 1 Har. & G. (Md.) 324; Rex v. Head, 4 Burr. 2515 (1770).

[7] Lockwood v. Mechanics' Nat'l Bank, 9 R. I. 308; Dunston v. Imperial, etc., Co., 3 B. & Ad 125.

making of all by-laws. Thus, a by-law must not be repugnant to the charter,[1] nor should it be a mere repetition or restatement of the provisions of the charter.

§ 149. **Must not be repugnant to law of the land.**—By-laws which are contrary to the law of the land are void. "Not only does a general and express legislative authority to make by-laws not authorize the passage of such as are in contravention of the law of the land,[2] but the legislature can not in any instance so far delegate its powers as to confer upon a corporation authority to enact by-laws which within the sphere of their operation would be practically a repeal of the statutes of the state or an abrogation of the common law."[3]

§ 150. **Public policy.**—A by-law which is against public policy, as one in general restraint of trade, is void.[4] But restraints particular as to time and place, if founded upon sufficient consideration, are valid.[5]

§ 151. **Must be reasonable.**—A valid by-law must be reasonable, and the question of reasonableness is one of law and not of fact.[6] The unreasonableness of a by-law should be demon-

[1] Bergman v. St. Paul, etc., Assn., 29 Minn. 275; Diligent, etc., Co. v. Com., 75 Pa. St. 291; Brewster v. Hartley, 37 Cal. 15, 99 Am. Dec. 237; Kolff v. St. Paul, etc., Exchange, 48 Minn. 215; President, etc., Assn. v. Allen, 105 Ind. 593; Supreme Council v. Perry, 140 Mass. 580; King v. Int.,etc., Assn., 170 Ill. 135. A by-law may be valid in part and invalid in part. Amesbury v. Bowditch, etc., Co., 6 Gray (Mass.) 596.

[2] Kennebec v. Kendall, 31 Me. 470.

[3] Beach, 1 Priv. Corp., § 312; Kent v. Quicksilver, etc., Co., 78 N. Y. 159; Seneca County Bank v. Lamb, 26 Barb. 595; In re Lighthall Mfg. Co., 47 Hun 258. A by-law establishing a rule in regard to sales different from the common law rule was held valid. Goddard v. Merchants' Exchange, 9 Mo. App. 290.

[4] Matthews v Associated Press, 136 N. Y. 333, and cases cited in note 1, p. 169; Mitchell v. Reynolds, 1 P. Wm. 181. A by-law may limit the time within which a suit may be brought, but can not absolutely forbid the bringing of an action. Nute v. Hamilton, etc., Co., 6 Gray 174.

[5] Gunmakers, etc., Co.v. Fell, Willes, 384; People v. Board of Underwriters, 54 How. Pr. 240. Must not be in restraint of personal liberty. Taylors of Ipswich, 11 Coke's Rep. 53.

[6] Com. v. Worcester, 3 Pick. 462; Cartan v. Father Mathew, etc., Society, 3 Daly 20; Hibernia, etc., Co. v.

strably shown. Courts in construing by-laws will hold them to be reasonable, if possible, not scrutinizing their terms for the purpose of making them void, nor holding them invalid if every particular reason for them does not appear.

§ 152. **Must be general.**—By-laws must be general—"directed to all within the sphere of their operation, and must operate equally."[1]

§ 153. **Effect of by-laws—As to members and officers.**—A member of a corporation is presumed to know of, and is bound by, all valid by-laws, rules or regulations to which he has assented, and his assent is presumed from his becoming a member of the corporation.[2] A stockholder is bound by all the

Harrison, 93 Pa. St. 264. In Kent v. Quicksilver, etc., Co., 78 N. Y. 159, Folger, J., said: "All by-laws must be reasonable, and consistent with the general principles of the law of the land, which are to be determined by the courts where a case is properly before them. A by-law may regulate or modify the constitution of a corporation, but can not alter it. The alteration of a by-law is but the making of another upon the same matter. If the first must be reasonable and in accord with the principles of law, so must that which alters it. If, then, the power is reserved to alter, amend, or repeal, and that reservation enters into a contract, the power reserved is to pass reasonable by-laws agreeable to law. But a by-law that will disturb a vested right is not such; and it differs not when the power to make and alter by-laws is expressly given to a majority of the stockholders, and that the obnoxious ordinance is passed in due form." A by-law to the effect that one who is an attorney in an action against the corporation is not eligible to the office of director is reasonable. Cross v. West Va., etc., R. Co., 37 W. Va. 342, 16 S. E. Rep. 587. In Bergman v. St. Paul, etc., Assn., 29 Minn. 275, the court said: "The authority to pass by-laws is, as a matter of course, authority to pass such as are consistent with the articles of incorporation, and not a power to subvert the law of corporate existence. The by-laws of a corporation are only rules and regulations as to the manner in which the corporate powers shall be exercised Any attempt on the part of defendant, by by-laws or otherwise, to deprive an unconsenting stockholder of a right secured to him by the corporate articles, is in excess of defendant's authority, or, in legal parlance, *ultra vires*" Sargent v. Franklin, etc., Co., 8 Pick. 90; Hibernia, etc., Co. v. Harrison, 93 Pa. St. 264. In Lynn v. Freemansburg, etc., Assn., 117 Pa. St. 1, a by-law providing for cumulative fines was held void as "oppressive, extortionate and unreasonable."

[1] Goddard v. Mer. Exch., 9 Mo. App. 290; Budd v. Multnomah, etc., R. Co., 15 Ore. 413.

[2] Frank v. Morrison, 58 Md. 423; Douglass v. Merchants', etc., Co., 118

by-laws in force when he became a member, although he had no actual knowledge of their existence.[1] A by-law which reserves a lien on the stock in favor of the corporation is binding on the stockholders if authorized by statute, or consented to by the stockholders.[2] Mere failure to object to the passage of an illegal by-law does not estop a stockholder from objecting when it is sought to enforce it against him.[3] The consideration of such assent is found in the privilege of becoming a member of the corporation.[4] Thus, a person who becomes insured in a mutual insurance company is a member of the company and bound by the by-laws, and chargeable with notice of them.[5] The general rule undoubtedly is, that where a policy is issued by a mutual insurance or benefit society, the assured, by virtue of his insurance, becomes a member of the society, and must take notice of and is bound by its articles of association and by-laws, although not recited in the policy, or expressly made a part of it. All the provisions of the by-laws not inconsistent with the provisions of the policy itself will be binding as a part of the contract. But when a by-law and the policy issued are in conflict, the company must be deemed to have waived the provisions of the by-law in favor of the insured, and the provisions of the policy

N. Y. 484, 7 L. R. A. 822; McFadden v. Los Angeles Co., 74 Cal. 571; Austin v. Searing, 16 N. Y. 112, 69 Am. Dec. 665. Members of mutual insurance and benefit societies are bound to take notice of the by-laws. Pfister v. Gerwig, 122 Ind. 567; Supreme Lodge K. of P. v. Knight, 117 Ind. 489, 3 L. R. A. 409; Supreme Com., etc., v. Ainsworth, 71 Ala. 436, 46 Am. R. 332; Walsh v. Ætna, etc., Co., 30 Iowa 133, 6 Am. R. 661; Treadway v. Hamilton, etc., Co., 29 Conn. 68; Simeral v. Dubuque, etc., Co., 18 Iowa 319. But it has been held that only such by-laws as are referred to in the policy are binding on the policy-holder. Kingsley v. New England, etc., Co., 8 Cush. (Mass.) 393; Miller v. Hillsborough, etc., Co., 44 N. J. Eq. 224. See Brent v. Bank of Wash., 10 Pet. (U. S.) 594.

[1] Matthews v. Associated Press, 136 N. Y. 333; Treadway v. Hamilton, etc., Co., 29 Conn. 68; Green v. Board of Trade, 174 Ill. 585, 51 N. E. Rep. 599; Board of Trade v. Nelson (Ill.), 44 N. E. Rep. 741; In re Haebler (N. Y.), 44 N. E. Rep. 87.

[2] Atchison Co. Bank v. Durfee, 118 Mo. 431. But see Brinkerhoff-Farris Trust & S. Co. v. Home L. Co., 118 Mo. 447, Wilgus' Cases.

[3] Kolff v. St. Paul Fuel Ex., 48 Minn. 215.

[4] Palmetto Lodge v. Hubbell, 2 Strob. (S. C.) 457.

[5] Pfister v. Gerwig, 122 Ind. 567; Mitchell v. Lycoming, etc., Co., 51 Pa. St. 402; Treadway v. Hamilton, etc., Co., 29 Conn. 68; Coles v. Iowa, etc., 18 Iowa 425.

will govern the rights of the parties.[1] There is a conflict in the authorities as to the power of a mutual insurance company to change its by-laws in such a manner as to affect an existing contract of insurance.[2] "Where by-laws are for any reason illegal, it will not be presumed that the stockholders have assented to them, and even if they expressly assent they are not bound by such by-laws."[3] Thus, a stockholder can not be deprived of his membership by reason of an illegal by-law, although he assented to it.[4] A stockholder who signed a by-law which pledged the members to be liable "in their individual as well as their collective capacities," for money lent to the corporation, was held not personally liable for money subsequently loaned to the corporation where there was no evidence that the money was advanced on the credit of the by-law, other than the fact that the preamble of the by-law stated that the object of the corporation was to afford persons desirous of saving their money means of employing it to advantage.[5] By-laws which are adopted by stockholders are binding upon the directors with a force equal to that of the charter of the corporation and the statutes of the state. They have no power to modify or waive them; but a by-law made by the directors under proper authority may be waived or modified by them.[6] By-laws are binding upon the officers of a corporation, although they may not be stockholders in the corporation. They are presumed, by reason of their relation to the corporation, to have knowledge of the by-laws, and to

[1] Davidson v. Old People's, etc., Soc., 39 Minn. 303, 1 L. R. A. 482, annotated; Clark v. Mutual, etc., Assn. (D. C.), 43 L. R. A. 390.

[2] That the contract is subject to change, see Dwenger v. Geary, 113 Ind. 106; Supreme Lodge v. Knight, 117 Ind. 489; Stohr v. San Francisco, 82 Cal. 557; Supreme Commandery v. Ainsworth, 71 Ala. 436. *Contra:* Mut. Ben. Assn. v. Warner, 24 Ill. App. 357; Mut. Endow. Soc. v. Essenden, 59 Md. 463.

[3] In re Klaus, 67 Wis. 401; Thomas v. Mut., etc., Union, 17 N. Y. St. Rep. 51, 49 Hun (N. Y.) 171. But see, *contra*, Skelly v. Private, etc., Soc., 13 Daly (N. Y.) 2; Great Falls, etc., Co. v. Harvey, 45 N. H. 292; Hibernia, etc., Co. v. Harrison, 93 Pa. St. 269.

[4] People v. St. Franciscus, etc., Soc., 24 Howard's Pr. (N. Y.) 216.

[5] Flint v. Pierce, 99 Mass. 68.

[6] Campbell v. Merchants', etc., Co., 37 N. H. 41.

accept their offices with relation thereto.[1] A shareholder is not chargeable with constructive notice of resolutions adopted by the board of directors, "or by provisions in the by-laws regulating the mode in which its business shall be transacted with its customers."[2]

§ 154. **Effect upon third persons.**—A person who is not a member or an officer of a corporation is not bound by its by-laws, of which he has no notice, nor can he claim rights based upon such as are mere rules for the government of the officers and members in the management of the affairs of the corporation.[3] "Strangers to the company can not be bound by the rules adopted for the government of the company."[4] A by-law can not impose obligations upon persons who contract with a corporation without reference to or knowledge of it. Thus, one who purchases in good faith the stock of a corporation is not affected by a lien on the stock in favor of the corporation which was created by a by-law of which he had no notice.[5] So one dealing with the agent of a corporation is not bound by a by-law creating a limitation upon the apparent authority of the agent, of which he had no notice.[6] But one who has knowledge of a by-law deals with reference to it;[7] and, unless such a by-law is expressly excluded, it enters into a contract.[8] Thus, one who contracts to serve a corporation at a yearly salary, with

[1] Bank of Wilmington v. Wollaston, 3 Harr (Del.) 90; Hunter v. New Orleans, etc., Co., 26 La. Ann. 13; Douglass v. Merchants', etc., Co., 118 N.Y. 484.

[2] Pearsall v. Western, etc., Co., 124 N. Y. 256.

[3] McFadden v. Los Angeles Co., 74 Cal. 571; Cummings v. Webster, 43 Maine 192; Austin v. Searing, 16 N. Y. 112, 69 Am. Dec. 665, annotated; Rathbun v. Snow, 123 N. Y. 343, 10 L. R. A. 355, note; Fay v. Noble, 12 Cush. (Mass.) 1.

[4] Smith v. Smith, 62 Ill. 496.

[5] Bank, etc., v. Pinson, 58 Miss. 421, 38 Am. Rep. 330; Driscoll v. Manufacturing Co., 59 N. Y. 96; Anglo, etc., v. Grangers, etc., 63 Cal. 359. A person holding stock is bound by notice of such a by-law, printed on the certificate. State, etc., Assn. v. Nixon-Jones, etc., Co., 25 Mo. App. 642.

[6] Rathbun v. Snow, 123 N. Y., 343; Hallenbeck v. Powers, etc., Co. (Mich.), 76 N. W. Rep. 119; Moyer v. East Shore, etc., Co., 41 S. C. 300, 25 L. R. A. 48, and note on effect of by-laws as notice.

[7] Hallenbeck v. Powers, etc., Co. (Mich.), 76 N. W. Rep. 119.

[8] Barbot v. Mutual, etc., Assn. 100 Ga. 681, 28 S. E. Rep. 498.

knowledge of a by-law which provides that his office should be held at the pleasure of the board of directors, is bound thereby.[1] If the effect of such by-law is to be excluded, it must be by special contract, made with competent authority.[2] "The office of a by-law is to regulate the conduct and define the duties of the members towards a corporation and between themselves; so far as its provisions are in the nature of contract, the parties thereto are the members of the association between themselves; or the corporation on the one side and its individual members on the other. The right of any third party, stranger to the association, to establish a legal claim through such a by-law, must depend upon the general principles applicable to express contracts."

§ 155. **By-laws limiting powers of agents.**—The authorities are conflicting upon the question of the effect of a by-law which limits the apparent powers of an officer of a corporation. The rule most consistent with reason and supported by the weight of authority seems to be that the powers of officers of manufacturing and trading corporations can not be limited to those enumerated in the by-laws as against persons dealing with them without notice of the limitations. Such persons are justified in assuming that the officers have the authority implied in their designations.[3] The contrary rule was adopted in a line of New York cases,[4] but these were in effect reversed by the court of appeals, which in a recent case[5] held that the by-laws

[1] Douglas v. Insurance Co., 118 N. Y. 484.

[2] Flint v. Pierce, 99 Mass. 68; Trustees v. Shaffer, 63 Ill. 243.

[3] Fay v. Noble, 12 Cush. 1; Smith v. Smith, 62 Ill. 496; Moyer v. East Shore, etc., Co., 41 S. C. 300, 25 L. R. A. 48; Wait v. Smith, 92 Ill. 385; Union, etc., Co. v. White, 106 Ill. 67; Walker v. Wilmington, etc., R. Co., 26 S. C. 80; Arapahoe, etc., Co. v. Stevens, 13 Colo. 534; Ten Broek v. Winn Boiler, etc., Co., 20 Mo. App. 19; Donovan v. Halsey, etc., Co., 58 Mich. 38.

[4] Adriance v. Roome, 52 Barb. (N. Y.) 399; De Bost v. Albert Palmer Co., 35 Hun (N. Y.) 386; Dabney v. Stevens, 10 Abb. Pr. N. S. 39; Smith v. Co-Op., etc., Assn., 12 Daly 304; Westerfield v. Radde, 7 Daly 326; Bohm v. Loewer's, etc., Co., 30 N. Y. S. R. 424; Rathbun v. Snow, 22 N. Y. S. R. 227. See, also, Bocock v. Allegheny, etc., Co., 82 Va. 913; Haden v. Farmers', etc., Co., 80 Va. 691.

[5] Rathbun v. Snow, 123 N. Y. 343, 10 L. R. A. 355.

of a business corporation are binding only upon such persons as deal with the corporation with knowledge of their existence. Third persons may act upon the apparent authority conferred by the principal upon the agent, and are not bound by secret limitations or instructions qualifying the terms of the written or verbal appointment. Hence, said the court: "The defense based upon the limitation in the by-laws of the company, of which the plaintiff had no knowledge, can not be sustained. By-laws of business corporations are, as to third persons, private regulations, binding as between the corporation and its members, or third persons having knowledge of them, but of no force as limitations *per se* as to third persons, of an authority, which, except for the by-law, would be construed as within the apparent scope of the agency."

§ 156. **Rules and regulations published by corporations.**— The *by-laws* of a private corporation "bind the *members only* by virtue of their assent, and do not affect third persons. All regulations of a company affecting its business, which do not operate upon third persons, are properly denominated by-laws of the company, and may come within the operation of the principle. Within this limit it is the peculiar and exclusive office of the court to decide upon the validity of the regulation. But there is another class of regulations, made by corporations as well as individuals who are common carriers of passengers, which operate on and affect the rights of others, which are not, properly speaking, by-laws of the corporation, and which do not fall within the operation of this principle. Of this character are all regulations touching the comfort and convenience of travelers, or prescribing rules for their conduct to secure the just rights of the company."[1] To this class belongs the rules adopted by savings banks prescribing the rights of depositors and the methods of withdrawing funds. Depositors are presumed to assent to these rules, and are bound by them. The fact that the depositor is unable to read the rules printed in the pass-book does not defeat its effect as notice.[2]

[1] State v. Overton, 24 N. J. L. 435, Wilgus' Cases.

[2] Burrill v. Dollar, etc., Bank, 92 Pa. St. 134, 37 Am. Rep. 669; People's,

§ 157. **By-laws imposing forfeiture.**—A forfeiture of stock for non-payment of calls and assessments was unknown to the common law[1] and can only be exercised by virtue of statutory authority. In the absence of a grant in the charter of power of forfeiture, a by-law authorizing a forfeiture is invalid,[2] but a stockholder may consent that his stock may be forfeited for non-payment of calls or assessment, and when the contract is indorsed upon his certificate of stock it is binding.[3] When the power of forfeiture is conferred by the charter and the manner of exercising such power is prescribed by a by-law, a sale made in any other manner than as so provided is unlawful. "A by-law of defendant's association, also made one of the terms and conditions of the stock certificates, as the same were printed and issued, requiring and providing for a sale at public auction, in case of a failure to meet the prescribed monthly payments for a period of six months, was ignored and disregarded, to the extent that the sale was in the directors' room in the offices of the corporation, and no open, public, or general notice of the same was ever given. By the same by-law it was also provided that, whenever any stock was to be sold for arrearages in the monthly payments, a notice should be mailed to the owner of the stock ten days, at least, before the day of sale, stating the time and place of such sale. This express and important provision was also ignored and disregarded, and the sales made without any attempt to notify stockholders in default, by mail or in any other manner. Hence the sales were irregular and unlawful."[4]

§ 158. **Expulsion of members.**—A corporation may adopt reasonable rules for the regulation of the conduct of its members in carrying out their agreements, and may provide for

etc., Bank v. Cupps, 91 Pa. St. 315; Supreme Commandery v. Ainsworth, 71 Ala. 436.

[1] § 387, *infra*. Minnehaha, etc., Assn. v. Legg, 50 Minn. 333; Westcott v. Minn., etc., Co., 23 Mich. 145; Budd v. Multnomah, etc., R. Co., 15 Ore. 404, 15 Pac. Rep. 659.

[2] In re Long Island R. Co., 19 Wend. 37. But see Elizabeth City Cotton Mills v. Dunstan, 121 N. C. 12, 61 Am. St. R. 654.

[3] Weeks v. Silver, etc., Co., 23 J. & S. (N. Y.) 1.

[4] Allen v. Am., etc., Assn., 49 Minn. 544.

the expulsion of a member for non-compliance with a contract entered into with another member, although the contract was void under the statute of frauds.[1]

Such organizations as clubs, benevolent societies, stock and commercial associations, may make by-laws providing for the expulsion of members who have violated obligations imposed upon them by virtue of their membership.[2] But in corporations owning property there is no power to expel a member unless expressly conferred by the charter.[3] Such authority can not be conferred by a by-law.[4] The remedy for unlawful expulsion is by mandamus to compel restoration to membership.[5]

§ 159. **Amendment, repeal and waiver.**—The same authority which makes a by-law may amend or repeal it,[6] and members are bound by amendments made in accordance with existing rules to the same extent as by the original by-law.[7] Where articles of incorporation are void they can not be made good by amendment, although the amended articles are properly filed.[8] An amendment can not be affected by a usage contrary to a by-law.[9] A corporation may by a course of dealing waive a by-law, and be unable to assert it against those with whom it deals.[10] But the officers can not waive by-laws

[1] See Ch. XII. Dickenson v. Chamber of Com., 29 Wis. 45; State v. Chamber of Com., 47 Wis. 670; Goddard v. Merchants' Exchange, 9 Mo. App. 290, 78 Mo. 609; Gregg v. Mass. Med. Society, 111 Mass. 185; Southern, etc., Co. v. Hixon, 5 Ind. 165.

[2] People v. Board of Trade, 80 Ill. 134; Hussey v. Gallagher, 61 Ga. 86; Dawkins v. Antrobus, L. R. 17 Ch. Div. 615. Compare State v. Williams, 75 N. C. 134.

[3] Evans v. Phila. Club, 50 Pa. St. 107; State v. Chamber of Com., 47 Wis. 670; Dickenson v. Chamber of Com., 29 Wis. 45.

[4] People v. St. F. Ben. Society, 24 How. Pr. 216 (N. Y.); Roehler v. Mech. Aid Society, 22 Mich. 86.

[5] People v. Musical, etc., Union, 118 N. Y. 101; State v. Carteret Club, 40 N. J. L. 295.

[6] Heintzelman v. Druid, etc., Assn., 38 Minn. 138.

[7] Poultney v. Bachmann, 31 Hun 49; McDowell v. Ackley, 93 Pa. St. 277.

[8] State v. Critchett, 37 Minn. 13; State v. Truby, 37 Minn. 97.

[9] Sills v. Brown, 9 Carr & P. 604.

[10] Clark v. Insurance Co., 6 Cush. 342; Susquehanna, etc., Co. v. Elkins, 124 Pa. St. 481; Cumberland, etc., Co. v. Schell, 29 Pa. St. 31; Splawn v. Chew, 60 Tex. 532; Manning v. Ancient, etc., 86 Ky. 136, 5 S. W. Rep. 385.

which were adopted by the stockholders for the protection of the corporation.[1]

II. Power to Take and Hold Land.

§ 160. **The common law rule.**—Blackstone names as one of the incidental powers of every private corporation the power to acquire and hold real estate. At common law every private corporation had implied power to take and hold such lands only as were reasonably necessary for the purposes of its creation.[2] This limitation, it has been said, was imposed by the common law independent of statute,[3] but probably was not so, if the king's license in mortmain was obtained.[4]

§ 161. **Statutory restrictions.**—By the English statutes of mortmain, beginning with *Magna Charta* and ending with 9 George II, all corporations were forbidden to take and hold

[1] Mulrey v. Insurance Co., 4 Allen (Mass.) 116.

[2] 1 Blk. Com., p. 478; 2 Kent Com., pp.227, 281; Nicoll v. Railway Co., 12 N. Y. 121; Thompson v. Waters, 25 Mich. 214; Blanchard v. Warner, 1 Blatchf. U. S. 258; Page v. Heineberg, 40 Vt. 81, 94 Am. Dec. 378; McCartee v. Orphans' Asylum Soc., 9 Cow. (N.Y.) 437, 18 Am. Dec. 516; Rivanna, etc., Co. v. Dawson, 3 Grat. (Va.) 19, 46 Am. Dec. 183; Mallett v. Simpson, 94 N. C. 37, 55 Am. Rep. 594. 1 Kyd. Corp., 79, citing 19 Henry VI, 44, says that at common law corporations had the same capacity to take and hold lands as a private person prior to Magna Charta (1215). A corporation has no power to purchase or take either real or personal property by gift, devise or bequest for an unauthorized purpose. Hence, under authority, to take lands for a right of way and certain enumerated purposes, a railway corporation can not take lands by donation for purposes in no way connected with the road. Case v. Kelly, 133 U. S. 21. The presumption is in favor of the right of the corporation to hold real estate. People v. Larue, 67 Cal. 526; Stockton Bank v. Staples, 98 Cal. 189. A corporation with legal capacity to take and hold property may take and hold it in trust, when authorized by law, to the same extent as a private person. White v. Rice (Mich.), 70 N. W. Rep. 1024.

[3] State v. Com'rs, 23 N. J. L. 510, 57 Am. Dec. 409. The real estate must be held for a purpose which tends to carry out the object for which the corporation was created. Thus, in the absence of a prohibitory law, a corporation formed for religious purposes may hold land as a trustee for such uses. Phillips Academy v. King, 12 Mass. 564. A corporation formed for educational purposes may hold lands in aid thereof. Phillips Academy v. King, 12 Mass. 564. See Regents v. Detroit, etc., Soc., 12 Mich. 138; Leggett v. Ladd, 23 Ore. 26. As to power of alienation at common law, see note, 7 Eng. Rul. Cas. 377, and cases cited.

[4] Angell & Ames Corp., 8th ed., § 145

land without a license from the crown.[1] These statutes were never re-enacted in the United States,[2] and were not in force in any state, except under certain restrictions, in Pennsylvania.[3] The various states have, however, generally adopted constitutional or statutory restrictions which limit the power of corporations in this respect.[4] These statutes ordinarily grant to corporations power to "acquire, hold and transfer all such real and personal estate as is necessary or convenient for the purpose of conducting, carrying on or disposing of the business of such corporation."[5] The acquisition of real estate for purposes

[1] 2 Kent Com., p. 282; 1 Washburn Real Property, 4th ed., p. 76.

[2] Moore v. Moore, 4 Dana (Ky.) 354, 29 Am. Dec. 417; Rivanna Nav. Co. v. Dawson, 3 Grat. (Va.) 19, 46 Am. Dec. 183; Mallett v. Simpson, 94 N. C. 37, 55 Am. Rep. 594.

[3] Leazure v. Hillegas, 7 Serg. & R. (Pa.) 313. In In re McGraw's Estate, 111 N. Y. 67, the cases are reviewed. The court said: "As at common law a corporation could take real property in the same way as an individual; the consequence was that, in England, large landed possessions were held by religious corporations, and, by reason of alienations of real estate to them, the services due by the vassal to the lord were partially if not totally paralyzed, and the chief lords lost their escheats. This was a constantly growing and alarming evil. To remedy the evil, the first Mortmain act was placed in Magna Charta, which declared all such alienations to corporations entirely void, and that the lands should revert to the lord of the fee. It was held, however, that the reversion must be accompanied by an entry, and then, and from that time, there was a forfeiture, the corporation having taken the title and held the property until such forfeiture by re-entry. Shelf. Mortm. 8, 31; 1 Kyd. Corp. 81; Grant Corp. 106. Other statutes upon the subject were subsequently enacted, all for the purpose of preventing the great accumulation of real property in the hands of corporations, and they all provided substantially for a re-entry on the part of the next superior lord whenever lands had been aliened in mortmain; and, until such entry enforcing the forfeiture, the corporation held the lands. There was one law, directed against superstitious uses (23 Henry VIII, c. 10), which provided that the grant to such uses for more than twenty years was absolutely void, and the estates thus aliened would have gone to the grantor or his heirs, excepting for a provision subsequently made, giving such estates to the king. Wilm., notes, 9, 10, in Attorney-General v. Downing, variously reported: Amb. 550, 571; 1 Dick. 414; 3 Ves. 714; 5 Ves. 300; 8 Ves. 256. The mortmain statute (9 Geo. II., c. 36) renders all devises to charitable uses void. Shelf. Mortm. 118–120."

[4] Gilbert v. Hole, 2 S. Dak. 164; Leggett v. N. J., etc., Co., 1 N. J. Eq. 541, 23 Am. Dec. 729. It is against public policy for a corporation to own more real estate than is necessary for the transaction of its corporate business or is required in the collection of debts. People v. Pullman, etc., Co., 175 Ill. 125.

[5] Gen. Stat. Minn., chap. 34, § 113. See First M. E. Church v. Dixon (Ill.),

foreign to the general objects of the corporation is, under such statutes, an *ultra vires* act. Thus, a corporation organized for manufacturing purposes may acquire real estate upon which to locate its buildings or plant, but it can not purchase lots for speculative purposes.[1] A corporation authorized by its charter to hold real property, may lease it to be used for a business which the corporation itself could not lawfully carry on.[2] The quantity of real estate which a foreign corporation may hold is generally restricted by statute.[3] Under such a statute it can not indirectly own the land by holding the majority of the stock of a domestic corporation.[4]

§ 162. **Distinction between the power to take and to hold.**— Although the authorities are not uniform, the preponderance is in favor of the proposition that a prohibition on the power to hold real estate does not exclude the power to take the title to real estate subject to the risk of being ousted by the state.[5] This appears to have been the English rule,[6] and under it the corporation may at any time previous to a judgment of ouster, convey a good and valid title. There are many cases, however, which hold that a corporation which is forbidden to hold real estate can not take the title, and that a conveyance or a

52 N. E. Rep. 887. For construction of such statutes, see Crawford v. Longstreet, 43 N. J. L. 325; Belcher v. St. Louis, etc., Co., 101 Mo. 192, 13 S. W. Rep. 822.

[1] Case v. Kelly, 133 U. S. 21; Commonwealth v. Railway Co., 132 Pa. St. 591; Matthews v. Skinker, 62 Mo. 329; Commonwealth v. Railway Co., 139 Pa. St. 457; Freeman v. Sea View, etc., Co., N. J. Eq. 40 Atl. Rep. 218.

[2] Nye v. Storer, 168 Mass. 53, 46 N. E. Rep. 402.

[3] American, etc., Co. v. Tennille, 87 Ga. 28; Koenig v. Chicago, etc., R. Co., 27 Neb. 699.

[4] The reasons for such restriction are well stated by Christiancy, J., in Thompson v. Waters, 25 Mich. 214.

Where the value of the real estate which a corporation may hold is limited, the title is not divested by an increase in the value beyond the prescribed amount. Bogardus v. Trinity Church, 4 Sandf. Ch. 633; Harvard College v. Boston, 104 Mass. 470; Comw. v. N. Y., etc., Co., 114 Pa. St. 340. See generally: Tarpey v. Desert, etc., Co., 5 Utah 494, 17 Pac. Rep. 631; Boyce v. St. Louis, 29 Barb. 650; Starkweather v. Am., etc., Soc., 72 Ill. 50; Am., etc., Soc. v. Marshall, 15 Ohio St. 537.

A devise of land to the government of the United States is void. United States v. Fox, 94 U. S. 315.

[5] Thompson Priv. Corp., § 5775.

[6] See Leazure v. Hillegas, 7 Serg. & Raw. (Pa.) 313, Wilgus' Cases.

devise to it is of no effect.[1] In accordance with this rule, it was held that a devise of real estate to a corporation which, by reason of this limitation upon its power, was unable to hold it, was of no effect, and that the title vested in the heirs.[2]

§ 163. **Manner of acquiring title.**—By the common law a corporation could acquire title to real estate the same as an individual.[3] So under the modern law it may acquire title in any way that a natural person can, as by adverse possession,[4] devise,[5] prescription, or by the exercise of the power of eminent domain.[6] When a corporation has power to become a creditor, it may, unless expressly prohibited, take a mortgage upon real estate as security, and in case of default acquire title by foreclosure.[7] Thus, a railway corporation may take a mortgage upon real estate to secure the payment of subscriptions to its stock.

§ 164. **Power to take by devise.**—It is probable that the power to devise land was frequently exercised in Anglo-Saxon times, but after the Norman conquest, or at least after the feudal system was fully established, this method of alienating *lands* was not allowed to any one (except in a few places by local custom) until the Statute of Wills in the time of Henry VIII. But long before this time the *devise* of *uses* or *trusts* in land was recognized, so corporations could take an *use* in real estate by devise at common law;[8] but they were forbidden to hold the *land* itself, and after 15 Richard II, to hold the *use* (except by special license of the king), by a series of statutes extending from *Magna Charta* to 32 Henry VIII. The latter act, known as the statute of wills, provided that the sole owner of a fee simple could devise it to any one "except to bodies politic and corporate."[9] In the absence of such a statute of wills, or a restrictive statute of some kind, and subject to the rule that it must be reasonably necessary and convenient for carrying out the objects of the corporation, the old common law rule, that there is no inherent incapacity in a corporation to take by devise, prevails in the United States at the

[1] Wood v. Hammond, 16 R. I. 98; In re McGraw's Estate, 111 N. Y. 66, 2 L. R. A. 387.

[2] In re McGraw, 111 N. Y. 66.

[3] See Predyman v. Wodry, Crok. Jac. 109.

[4] Rehoboth v. Rehoboth, 23 Pick. (Mass.) 139.

[5] In re McGraw's Estate, 111 N. Y. 66.

[6] Thompson Priv. Corp., § 5589.

[7] Blunt v. Walker, 11 Wis. 334, 78 Am. Dec. 709.

[8] Porter's Case, 1 Co. Rep. 22, 24. See 1 Thomas's Co. Litt., p. 188, *et seq.*, note *g*; McCartee v. Orphan Asy. Soc., 9 Cow. 434, 18 Am. D. 516; Downing v. Marshall, 23 N. Y. 366, 80 Am. D. 290.

[9] This incapacity was removed by the statute of charitable uses (43 Eliz. C. 4 A. D. 1601), as regards gifts for various purposes therein denominated charitable.

present time.[1] A conveyance by a citizen of a state of property located in the state to a foreign corporation for benevolent purposes, when the state permits its own corporations to take real estate for like purposes, is valid. "In harmony with the general law of comity among the states composing the Union, the presumption should be indulged, that a corporation of one state not forbidden by the law of its being may exercise within any other state the powers therein granted, including the power of acquiring lands, unless prohibited therefrom, either in the indirect enactments, or by public policy deduced from the general course of legislation, or the settled adjudication of their highest courts."[2] When a statute of wills forbids a devise to a corporation, a devise of land in the state to a foreign corporation is void.[3] Judge Thompson says that the better rule is that the disability created by a statute of wills does not follow the corporation into another state, while a disability created by the charter or general corporation law follows the corporation everywhere.[4]

§ 165. **Devise to corporation—Statutory limit.**—The better rule is that the state only can raise the question that the corporation is holding more real estate than it is permitted to hold under the law.[5] We have already seen that the authorities are not uniform on the question of the power of a corporation which is forbidden to hold real estate to take title to the same.[6] It was recently held by the supreme court of Maine that a bequest to an incorporated charitable institution of property in excess of the amount which such corporations are allowed by general statutes to take and hold, there being no prohibition by the statute of wills, or the charter of the corporation, and no penalty for taking in excess of the limitation, is not void but merely voidable at the instance of the state.[7] But the New York Court of Appeals, in recent important cases, has held that a devise of an amount of land which, together with the amount already held, exceeding the statutory limit, is void as to the excess only. The title to the excess was held to vest in the heirs of the devisor, and they were permitted to raise the question of

[1] In re McGraw, 111 N. Y. 66; Downing v. Marshall, 23 N. Y. 366, 80 Am. Dec. 290.

[2] Christian Union v. Yount, 101 U. S. 352.

[3] Draper v. Harvard College, 57 Howard Pr. N. Y. 269.

[4] Corps., § 5785. But see Starkweather v. Am. Bible Soc., 72 Ill. 50, 22 Am. Rep. 133.

[5] American, etc., Soc. v. Marshall, 15 Ohio St. 537; Christian, etc., v. Yount, 101 U. S. 352.

[6] §§ 162, *supra*, 168, *infra*. De Camp v. Dobbins, 29 N. J. Eq. 36.

[7] Farrington v. Putnam, 90 Me. 405, 37 Atl. Rep. 652.

the right of the corporation to take the title.[1] A devise to a trustee to collect the rents and profits for the benefit of a corporation, which is forbidden to hold real estate, is a mere evasion of the statute and void.[2]

§ 166. **The doctrine of equitable conversion.**—When a corporation is incapable of taking a devise of real estate, the will may direct the executors to convert the real estate into money, and pay the proceeds over to the corporation. On well established principles, this is considered a bequest of money.[3]

§ 167. **The estate which may be taken.**—A corporation may take a title in fee-simple, although the period of the corporate existence is limited. Chancellor Kent said that a corporation has a fee-simple for the purpose of alienation, but only a determinable fee for the purpose of enjoyment, and that on the dissolution of the corporation, the reversion is to the original grantor or his heirs; that the grantor will be excluded by the alienation of the fee, and in that way the corporation may defeat the possibility of a reversion.[4] In modern times, upon the dissolution of a joint stock corporation, the title to its real estate passes into administration for the benefit of its creditors first and its stockholders afterwards.[5]

[1] In re McGraw's Estate, 111 N. Y. 66, 2 L. R. A. 387. And see Cornell, etc., v. Fiske, 136 U. S. 152; Wood v. Hammond, 16 R. I. 98.

[2] McCartee v. Society, 9 Cow. (N. Y.) 437. See Downing v. Marshall, 23 N. Y. 366; Coleman v. San., etc., Co., 49 Cal. 517

[3] Sherwood v. American Bible Soc., 1 Keyes (N. Y.) 561; Orrick v. Boehm, 49 Md. 72. As to the doctrine of equitable conversion generally, see Given v. Hilton, 95 U. S. 591. If the real estate is devised to the corporation, a court of equity can not convert it into money and direct the money paid over to the corporation. Starkweather v. Society, 72 Ill. 50.

[4] Kent's Com., 283; Nicoll v. Railway Co., 12 N. Y. 121; People v. Mauran, 5 Denio (N. Y.) 389; Page v. Heineberg, 40 Vt. 81; People v. O'Brien, 111 N. Y. 1, 7 Am. St. Rep. 684; Detroit St. R. Co. v. Detroit, 110 Mich. 384. A corporation may hold title to real estate as tenant in common with another corporation or natural person. New York, etc., Co. v. Fulton Bank, 7 Wend. (N. Y.) 412; 1 Washburn Real Property, 4th ed., 613. But not as joint tenant. Telfair v. Howe, 3 Rich. Eq. (S. C.) 235, 55 Am. Dec. 637.

[5] Heath v. Barmore, 50 N. Y. 302.

§ 168. **Who can question the right of the corporation.**—On grounds of public policy it is generally held that the state only can raise the question that a corporation which has power to hold land for any purpose, or under any circumstances, is holding real estate which it has no authority to hold.[1] The general rule is that the title of the corporation to real property can not be questioned by a private person, upon the ground that the law gives the corporation no right to take or hold such a title. Hence, a corporation which has received a grant of land may convey a good title to a grantee,[2] or maintain an action against trespassers,[3] although it has no legal right to hold real estate. This rule does not apply, however, when the corporation is seeking to acquire lands contrary to its charter.[4] The right of a corporation to take or hold land in violation of its charter will not be inquired into collaterally.[5]

[1] Congregational, etc., Soc. v. Everitt, 85 Md. 79, 36 Atl. Rep. 654, 35 L. R. A. 693; Water, etc., Co. v. Tenney, 24 Colo. 344, 51 Pac. Rep. 505; State v. Elizabeth (N. J.), 39 Atl. Rep. 683, 906; Lauder v. Peoria, etc., Soc., 71 Ill. App. 475; Cooney v. A. Booth, etc., Co., 169 Ill. 370, 48 N. E. Rep. 406; National Bank v. Whitney, 103 U. S. 99; Fritts v. Palmer, 132 U. S. 282; Hough v. Cook Co., etc., Co., 73 Ill. 23, 24 Am. Rep. 230; Hamsher v. Hamsher, 132 Ill. 273, 8 L. R. A. 556; Alexander v. Tolleston Club, 110 Ill. 65; Gilbert v. Hole, 2 S. Dak. 164, 49 N. W. Rep. 1; Mallett v. Simpson, 94 N. C. 37, 55 Am. Rep. 594; Ragan v. McElroy, 98 Mo. 349; Blunt v. Walker, 11 Wis. 334, 78 Am. Dec. 709; Hayward v. Davidson, 41 Ind. 212; American, etc., Co. v. Tennile, 87 Ga. 28; Tidwell v. Chiricahua, etc., Co., 53 Pac. Rep. (Ariz.) 192. The property is held subject to the state right of escheat. Hickory, etc., Co. v. Buffalo, etc., R. Co., 32 Fed. Rep. 22.

[2] Blunt v. Walker, 11 Wis. 334, 78 Am. Dec. 709; Farmers', etc., Co. v. Curtis, 7 N. Y. 466.

[3] Southern, etc., R. Co. v. Orton, 6 Sawy. (C. C.) 157.

[4] Case v. Kelly, 133 U. S. 21; Pacific R. Co. v. Seeley, 45 Mo. 212, 100 Am. Dec. 369.

[5] Shewalter v. Pirner, 55 Mo. 218; People v. Mauran, 5 Denio (N.Y.) 389; Ehrman v. Union, etc., Co., 35 Ohio St. 324; Cooney v. A. Booth, etc., Co., 169 Ill. 370.

CHAPTER 8.

PARTICULAR POWERS.

§ 169. Power to contract.
170. Manner of acting — Necessity for a seal.
171. Formalities to be observed in contracting.
172. Contracts which are against public policy.
173. Traffic agreements.
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185. Power to acquire personal property.
186. Power of alienation.
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188. Power to give a mortgage.
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199. The loaning of money.
199*a*. Power to act as a trustee.

§ 169. **Power to contract.**—For the purpose of advancing the objects of its creation a corporation may, subject to the limitations imposed by its charter, do whatever a natural person could do.[1] The power to make such contracts as are reasonably necessary in order to carry out its legitimate purposes inheres in every corporation, and is co-extensive with its corpo-

[1] Kelly v. Board, etc., 75 Va. 263; Blunt v. Walker, 11 Wis. 349; New England, etc., Co. v. Robinson, 25 Ind. 536. A corporation *de facto* may make any contract which the law authorizes a corporation to make. McTighe v. Macon, etc., Co., 94 Ga. 306, 32 L. R. A. 208.

rate powers.[1] But a corporation has no implied power to enter into contracts in aid of purposes other than those for which it was chartered,[2] and the general proposition is that it can enter into such contracts only as are expressly or impliedly authorized.[3] The fact that a particular contract may be advantageous to the corporation is immaterial. Where a railway company agreed to give a sum of money to aid in defraying the expenses of a musical festival, the agreement was held *ultra vires* and non-enforcible. The court said:[4] "Such a contract can not be held to bind the corporation by reason of any supposed benefit which it may derive from an increase of passengers over its road upon any grounds that would not hold it equally bound by a contract to partake in or to guarantee the success of any enterprise that might attract population or travel to any city or town upon its line." But a subscription by a hotel company to aid in bringing a military encampment to a town has been held valid.[5] A business corporation may make a valid contract to pay money to secure the location of a postoffice near its place of business.[6] A street railway company may bind itself by a note to aid in establishing a base-ball park where it will increase the traffic on the road.[7] These and many other cases which might be cited illustrate the general proposition that a corporate contract to be valid must be within the express or implied charter powers of the corporation.

§ 170. **Manner of acting.—Necessity for a seal.**—A corporation necessarily acts through its agents. The powers of the various corporate agents are discussed in another chapter, and it

[1] Portland, etc., Co.v. East Portland, 18 Ore. 21, 6 L. R. A. 290; McKiernan v. Lenzer, 56 Cal. 61.

[2] Chewacla, etc., Works v. Dismukes, 87 Ala. 344, 5 L. R. A. 100; Germantown, etc., Co. v. Dhein, 43 Wis. 420.

[3] Thomas v. Railroad Co., 101 U. S. 71; Davis v. Old Colony R. Co., 131 Mass. 258; Pearce v. Railroad Co., 21 How. (U. S.) 441; Franklin Co. v. Lewiston Inst., 68 Me. 43; Colman v. Railway Co., 10 Beav. 1; East Anglian R. Co. v. Eastern, etc., R. Co., 11 C. B. 775; Downing v. Mt. Washington, etc., Co., 40 N. H. 230.

[4] Davis v. Old Colony R. Co., 131 Mass. 258; Colman v. Railroad Co., 10 Beav. 1.

[5] Richelieu, etc., Co.v. Int., etc., Co., 140 Ill. 249.

[6] Green Co. v. Blodgett, 159 Ill. 169.

[7] Temple, etc., R. Co. v. Hellman, 103 Cal. 634.

is only necessary at this time to state that the corporation may, by rules or regulations in the form of by-laws, provide the manner in which its agents shall transact its business. These limitations are binding upon all who deal with the agents, with knowledge of the limitation, but in the absence of such knowledge the agent is conclusively presumed to have the power ordinarily appertaining to agents with such apparent authority. It may be taken as the rule that all persons are bound by knowledge of limitations which are contained in the charter or articles of incorporation, although it is difficult to see why an ordinary person is bound to know what is in a charter, granted by a special law, of which even a court will not take judicial notice.[1]

At common law a corporation could only enter into a contract by the use of its seal,[2] except in cases of comparatively little importance, such as the hiring of a servant, cook or butler.[3] But this rule was gradually relaxed. Trading companies were allowed to accept bills of exchange or execute a promissory note without affixing the corporate seal.[4] It was finally held that although the corporation could only contract under seal, it could, by a resolution not under seal, appoint an agent who could bind the corporation by his acts.

The question arose in Bank of Columbia v. Patterson,[5] and Mr. Justice Story, after stating the common law rule, said: "The technical doctrine that a corporation could not contract, except under its seal, or in other words, could not make a promise, if it had ever been fully settled, must have been productive of great mischiefs. Indeed, as soon as the doctrine was established that its regularly appointed agent could contract in their name, without seal, it was impossible to support it, for otherwise the party who trusted such contract would be without remedy against the corporation. Accordingly, it would seem to be a sound rule of law that wherever a corporation is

[1] This is based on the maxim of public policy that *ignorance of the law excuses no one*—the charter of a corporation whether under a general or a special act being considered a *law*.

[2] See cases cited in note to Doe v. Taniere, 12 Q. B. (Ad. and El. N. S.) 998, in 7 Eng. Rul. Cas. 366.

[3] Black. Com., Bk. I, ch. 18, 475.

[4] Horn v. Ivy, 1 Modern 18, Plow. 91 b; Church v. Coke Co., 6 Ad. and El. 846.

[5] 7 Cranch (U. S.) 298.

acting within the scope of the legitimate purposes of its institution, all parol contracts made by its authorized agents are express promises of the corporation; and all duties imposed on them by law, and all benefits conferred at their request, raise implied promises, for the enforcement of which an action will lie."[1]

In modern times a corporation is required to use a seal only when an individual must use one.[2] It is not necessary to the valid appointment of an agent.[3] A power of attorney to confess judgment[4] need not be under seal, nor it seems even for the purpose of conveying or mortgaging real estate of the corporation.[5] A corporation may be bound by the contracts of an agent which are neither authorized nor executed under the corporate seal.[6] As stated by Mr. Justice Story above: A corporation may be bound by an implied contract arising out of the acts of its agent, or from the acceptance of benefits, or from duties imposed by law.[7] The corporation may become liable by acquiescence. "Authority in the agent of a corporation may be inferred from the conduct of its officers, or from their knowledge and neglect to make objections, as well as in the case of individuals."[8] A provision in a statute that every contract of every corporation, by which a liability may be incurred by the company exceeding one hundred dollars, shall be in writing and under the seal of the corporation, or signed by some officer of the corporation authorized thereto, applies only to executory contracts. It has

[1] Bank of England v. Moffat, 3 Bro. Ch. 262; Rex v. Bank of England, Doug. 524 and note; Gray v. Portland Bank, 3 Mass. 364; Worcester, etc., Co. v. Willard, 5 Mass. 80.

[2] Crawford v. Longstreet, 43 N. J. L. 325.

[3] Bank v. Patterson, *supra;* Leekins v. Nordyke, etc., Co., 66 Iowa 471; Randall v. Van Vechten, 19 John. 60; Goodwin v. Screw Co., 34 N. H. 378; Hand v. Coal Co., 143 Pa. St. 408.

[4] Ford v. Hill, 92 Wis. 188, 66 N. W. Rep. 115.

[5] Dispatch Line v. Bellamy Mfg. Co., 12 N. H. 205; Fitch v. Steam Mill Co., 80 Maine 34; Cook v. Kuhn, 1 Neb. 472. But see Garrett v. Belmont Land Co., 94 Tenn. 459, Wilgus' Cases.

[6] Fletcher v. U. S. Bank, 8 Wheat. 358; Hoag v. Lamont, 60 N. Y. 96.

[7] Bank of Columbia v. Patterson, *supra;* Pixley v. West Pac. R. Co., 33 Cal. 183; Tyler v. Trustees, 14 Ore. 485; Hayden v. Middlesex T. Co., 10 Mass. 397; Gowen, etc., Co. v. Tarrant, 73 Ill. 608; Jones v. Nat., etc., Assn., 94 Pa. St. 215.

[8] Sherman v. Fitch, 98 Mass. 59.

no application when the company has received and retains the property.[1]

When a seal is attached it will be presumed to have been attached by competent authority. It has been said that a seal conclusively imports a consideration,[2] but the correct rule, as stated by Lord Campbell, is that "although the agreement be under seal we may examine to see whether there was any, and what consideration for the contract to pay money, when we are to determine whether the contract was or was not *ultra vires*."[3]

A bond, although for the payment of money, may be a negotiable instrument although under seal.[4]

§ 171. **Formalities to be observed in contracting.** Provisions prescribing the manner in which corporations shall do an act may be either directory or mandatory, depending upon the language of the statute and nature of the requirement. Mandatory directions as to the mode or form of entering into contracts must be followed.[5] But after a contract made in a different way is executed, and the corporation has received benefits under it, it may be compelled to pay for what it received.[6]

If a person dealing with a corporation has knowledge or is charged with notice that certain formalities are necessary on the part of the corporation, and are not being complied with, he may be unable to hold the corporation to the contract,[7] but if he has no such knowledge, and is not charged

[1] Roberts v. Deming, etc., Co., 111 N. C. 432; Pixley v. West Pac. R. Co., 33 Cal. 183; Curtis v. Mining Co., 109 N. C. 401.

[2] Royal Bank v. Grand Junction R. Co., 100 Mass. 445.

[3] Mayor of Norwich v. Norwich R. Co., 4 El. & Blk. 443.

[4] Am. Nat. Bank v. Am., etc., Co., 19 R. I. 149; Mercer Co. v. Hacket, 1 Wall. (U. S.) 83.

[5] Head v. Insurance Co., 2 Cranch. 127; Bissell v. Spring Valley Township, 110 U. S. 162; Topping v. Bickford, 4 Allen (Mass.) 120.

[6] Pixley v. West Pac. R. Co., 33 Cal. 183.

[7] Dana v. St. Paul Bank, 4 Minn. 385, Gil. 291; Leonard v. American Ins. Co., 97 Ind. 299; Head v. Providence Ins. Co., 2 Cranch. (U. S.) 127. Notice of restriction annexed to the grant of powers to a corporation is charged to persons dealing with the corporation. Smith v. Cornelius, 41 W. Va. 59, 30 L. R. A. 747.

with notice under the circumstances, his rights are not affected thereby.[1] One dealing with a corporate agent apparently having authority may properly assume, on the principle of right acting,[2] that the agent is acting within the scope of his real authority, that the corporation is acting regularly, and that all formalities and regulations with reference to the internal management and affairs of the corporation have been observed.[3]

§ 172. **Contracts which are against public policy.**—Corporations, like individuals, are forbidden to enter into contracts or agreements which the policy of the law considers detrimental to the public interest. Corporations charged with public duties are subject to restrictions of this nature which are peculiar and which grow out of the nature of the franchises granted them by the state. Their acts may be *ultra vires* because contrary to established principles of common law, or in violation of express statutes, such as have been enacted in most of the states.

§ 173. **Traffic agreements.**—It is settled law that agreements or arrangements between railway companies and other common carriers, which have for their object the prevention of competition, are void as against public policy; but this principle does not forbid all traffic arrangements. The rule is that "a business or traffic arrangement or contract entered into by a railroad or other corporation charged with the performance of public duties, which is fairly necessary, incidental, or ancillary to the carrying out of its purposes of incorporation, will be valid (assuming the contract to be entered into in the proper manner) provided the contract is not injurious to the public, (1) by necessarily or potentially rendering the corporation incapable of performing its public duties or enabling it to shirk its public obligations, or (2) by creating a monopoly in the contracting parties through the stifling of competition or in other ways,

[1] Insurance Co. v. McCain, 96 U. S. 84.

[2] Downing v. Mt. Wash. R. Co., 40 N. H. 230; Patterson v. Robinson, 116 N. Y. 193; Thomas v. Railroad Co., 101 U. S. 71.

[3] Hackensack Water Co. v. DeKay, 36 N. J. Eq. 548.

or (3) by giving exclusive or unfair advantages to certain individuals over the general public."[1] Subject to these restrictions, a railroad company may enter into a contract with shippers to carry beyond its own lines[2] and provide for dividing rates and freight under such circumstances.[3] The contract must not, however, be of such a nature as to amount to a practical transfer of the franchises of the corporation.[4]

§ 174. **Pooling arrangements—Contracts to prevent competition.**—Pooling arrangements between railway companies which have for their object the suspension of competition are, in the absence of express authority, *ultra vires* and void.[5] It is now settled that contracts of this character are invalid, without reference to the reasonableness of the rates established thereunder,[6] although it was held in New Hampshire[7] that a contract to prevent competition between railroad companies, but not for the purpose of raising the cost of transportation above reasonable rates, was valid. The court said: "It is equally free from doubt that when such contracts prevent an unhealthy competition and yet furnish the public with adequate facilities at fixed and reasonable rates, they are beneficial and in accord with sound principles of public policy."

[1] Taylor Private Corp., § 307.

[2] Railroad Co. v. Pratt, 22 Wallace U. S. 123.

[3] Elkins v. Camden, etc., R. Co., 36 N. J. Eq. 241; Stewart v. Erie, etc., Co., 17 Minn. 372.

[4] Ohio, etc., R. Co. v. Indianapolis, etc., R. Co., 5 Am. Law Reg. N. S. 733. "Corporations may make all necessary arrangements for cheaply and expeditiously developing and carrying on their particular business, but it is another thing to go beyond this, to enter into contracts for instance, by which the exclusive control of their exclusive right of working the line is handed over to other parties. All such arrangements, whatever their form, however disguised, are *ultra vires* and void." Green's Brice *Ultra Vires*, 339. For construction of a constitutional prohibition (Tex. Const., Art. 10, § 5), see G. C., etc., R. Co. v. State, 72 Tex. 404.

[5] Stewart v. Erie, etc., Co., 17 Minn. 372, Gil. 348; Gulf, etc., R. Co. v. State, 72 Tex. 404; Hartford, etc., R. Co. v. New York, etc., R. Co., 3d Robertson (N. Y.) 411.

[6] United States v. Freight Assn., 166 U. S. 290. As to the federal statute, see § 178, *infra*.

[7] Railroad Co. v. Railroad Co., 66 N. H. 100.

§ 175. **Contracts granting special privileges.**—Public policy forbids common carriers to make contracts by which special or exclusive privileges are given to one person or class of persons over others.[1] So there must be no undue or unreasonable discrimination between shippers in charges or facilities.[2]

§ 176. **Trust agreements.**—It may now be taken as settled that corporations can not without express authority enter into what have become known as trust agreements. Such contracts, whether made by formal corporate action or by the shareholders assuming to act in their individual capacities, but for the purpose of bringing the control of many corporations under one management, tend to stifle legitimate competition and create unlawful monopolies. Such contracts are *ultra vires*, and are also void on grounds of public policy. When a corporation enters into a trust, it is open to attack by the state on the ground (1) that it has attempted to grant away franchises conferred upon it in trust, the transfer being a breach of the implied condition that the particular grantee shall retain and execute the trust, and (2) that in making the contract, the result of which is the creation of a monopoly, it is guilty of an abuse of its franchises by employing them in the doing of an illegal act.[3] Corporations can be organized only for carrying on a lawful business, and as these combinations are unlawful and tend to create monopolies, the entering into them is sufficient ground for forfeiting the corporate charter in proceedings brought by the state for that purpose.[4] Whatever tends to create a monopoly or prevent competition amongst those engaged in business of a public character is illegal. It has been said a private manufacturing corporation stands on the same footing as an individual with

[1] Messenger v. Pennsylvania R. Co., 37 N. J. Law 531; Chicago, etc., R. Co. v. Suffern, 129 Ill. 274.

[2] Atchison, etc., R. Co. v. Denver, etc., R. Co., 110 U. S. 667; State v. C. N., etc., R. Co., 47 Ohio St. 130.

[3] People v. N. R. Ref. Co., 121 N. Y. 582.

[4] State v. Standard Oil Co., 49 Ohio St. 137; People v. N. R. Ref. Co., 121 N. Y. 582. See note on monopolies to People v. Chicago, etc., Co., 8 L. R. A. 497.

respect to its power to enter into contracts to limit production,[1] but the better rule would seem to be that the *corporation* can have its charter taken away for so doing, if the state sees fit to do so. The contract is therefore something more than void,—a violation of the corporate franchise also.[2] In order to forfeit a charter in *quo warranto* proceedings against the corporation for entering into a trust or illegal combination, it is not necessary to show actual public injury, as that will be presumed from the nature of the agreement.[3]

§ 177. **Illustrations of trust agreements.**—A manufacturing corporation formed for the purpose of buying up the plants of practically all other manufactories engaged in the same line for the purpose of pooling them and practically, if not wholly, preventing competition, enhancing prices, and producing a monopoly in a necessary article of food, is an illegal body, and has no standing in a court of equity.[4] Thus, the American Biscuit & Manufacturers Co. was organized as a corporation and issued a few shares to certain persons to qualify them as directors. It then began buying up plants and making payment therefor in its own stock. The defendant sold his bakery to the company and gave it possession, but took back a lease and entered into a contract by which he was to act as the agent of the company in conducting the business. He subsequently dispossessed the company, declared the scheme illegal, and in the litigation resulting it was held that the company had no rights which would be recognized by a court of equity,

[1] Oliver v. Gilmore, 52 Fed. Rep. 562.

[2] See People v. N. R. Sugar Ref. Co., 121 N. Y. 582, Wilgus' Cases,—a private sugar manufacturing company, and State v. Standard Oil Co., 49 Ohio St. 137,—a private manufacturing company. The complaint in both of these cases was that they had violated their corporate franchise in entering into such contracts and carrying them out. See also next section, 177.

[3] In Hilton v. Eckersley, 6 El. & Bl. 47, 65, Campbell, C. J., said: "I do not think that any averment is necessary as to what has been done under it, or as to any mischief which it has actually produced. We are to consider what may be done under it, and what mischief may thus arise."

[4] In National, etc., Co. v. Quick, 67 Fed. Rep. 130, the court said of the combination under consideration: "It seems to me that such a combination is illegal and that its purposes are violations of sound public policy. The common law forbids the organization of such combinations, formed of numerous corporations and firms. They are dangerous to the peace and good order of society, and they arrogate to themselves the exercise of powers destructive of the rights of free competition in the markets of the country, and by their aggregate power and influence imperil the free and pure administration of justice." Emery v. Candle Co., 47 Ohio St. 320; Santa Clara, etc., Co. v. Hayes, 76 Cal. 387, and cases cited in the following notes. Combination to fix the price of coal, see People v. Sheldon (N. Y.), 34 N. E. Rep. 785. For a general discussion and review of the authorities, see Atty.-Gen. v. Central R. Co., 50 N. J. Eq. 52–189, 24 Atl. Rep. 964, 25 Atl. Rep. 942.

as, under the guise of a manufacturing company, its real purpose was to combine the leading bakeries into a pool or trust.[1] Upon the same principle it was held that the Match Trust was invalid. The court refused to enforce the contract made in furtherance of a monopoly in corporate guise, although both sides to the controversy desired that the contract should be deemed valid. The court said:[2] "Large sums of money were used in buying up the various plants, greatly in excess of what they are worth; this was done to stop competition. These sums were called expenses, and were recouped by keeping up the prices of matches." So, a contract between a firm and a corporation and others, combining all the harrow-tooth manufactories, for the purpose of monopolizing the trade, was held illegal.[3] The Preserve Trust was held invalid on very broad grounds, the court holding that the corporation had no power to become a member of the trust or to place its property in the hands of trustees with power to purchase and control other plants.[4] In the Whisky Trust cases it was held that a corporation could not sell its entire property in furtherance of a monopoly.[5] A manufacturing corporation, formed for the purpose of providing commodities useful for the sustenance and maintenance of the people, can not without legislative authority delegate to a central body, whether incorporated or not, full control and management of the corporate affairs.[6] A contract between gas companies, fixing prices and pooling profits, and requiring one company not to extend its pipes in certain territory, is contrary to public policy, and void.[7] A

[1] American, etc., Co. v. Klotz, 44 Fed. Rep. 721.

[2] Richardson v. Buhl, 77 Mich. 632.

[3] Strait v. National, etc., Co., 18 N. Y. Sup. 224.

[4] American, etc., v. Taylor, etc., Co., 46 Fed. Rep. 152.

[5] State v. Nebraska, etc., Co., 29 Neb. 700; Distilling, etc., Co. v. People, 156 Ill. 448. "The object of the trust is clearly shown to have been illegal, as destroying competition and creating a most offensive monopoly, not only limiting the product, but also by dismantling as many distilleries as the trust saw fit, absolutely preventing the manufacture, except in a few controlled by the trust." Herschl, Consolidation, etc., p. 120.

[6] People v. N. R. Ref. Co., 121 N. Y. 582.

[7] Gibbs v. Consolidated, etc., Co., 130 U. S. 396; Chicago, etc., Co. v. People's, etc., Co., 121 Ill. 530; People v. Chicago, etc., Co., 130 Ill. 268.

corporation can not legally be organized for the purpose of controlling all other corporations engaged in a certain kind of business in a city.[1] A corporation formed to control the price of milk, or coal, is formed for an illegal purpose, and void.[2] But a contract between two water companies for co-operation in supplying water by which one officer of each company is appointed a trustee, the two to have general charge of the operation of the works, keeping account of receipts and expenditures, with a limited power of determining what should be charged to account of operating expenses with other powers simply directory, such as could not be discharged by a board of directors, except through an agent, is valid.[3] A combination for the control and prevention of competition in the sale of beer is not void at common law, although in restraint of trade, as beer is not an article of prime necessity, and its sale is closely restricted by public policy.[4]

§ 178. **Statutes forbidding trust agreements.**—Many states have passed statutes forbidding combinations which tend to prevent competition and create monopolies. The act of congress of July 2, 1890,[5] makes "every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce among the several states, or with foreign nations," illegal. The scope of this law was elaborately considered in the Trans-Missouri Freight Association case,[6] and it was held by a divided court that the agreement by which the association was created, although legal when made, was rendered invalid by the statute. "The language of the act," said the court, "includes *every* contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce among the several states, or with foreign na-

[1] People v. Chicago, etc., Co., 130 Ill. 268.

[2] People v. Milk, etc., 145 N. Y. 267; People v. Sheldon, 139 N. Y. 251.

[3] San Diego, etc., Co. v. San Diego, etc., Co., 108 Cal. 549, 29 L. R. A. 839.

[4] Anheuser-Busch, etc., Co. v. Houck (Tex.), 27 S. W. Rep. 692. But see Nester v. Brewing Co. (Pa. Sup.), 29 Atl. Rep. 102.

[5] 26 Stat. 209, C. 647.

[6] United States v. Trans-Mo., etc., Assn., 166 U. S. 290, Justices White, Field, Gray and Shiras dissenting. See the elaborate discussions in the Circuit Court of Appeals (19 U. S. App. 36) and in the District Court (53 Fed. Rep. 440), both holding contrary to the supreme court. See, also, United States v. Pipe Co., 85 Fed. Rep. 271.

tions. So far as the very terms of the statute go, they apply to any contract of the nature described. A contract, therefore, that is in restraint of trade or commerce is, by the strict language of the act, prohibited, even though such contract is entered into between competing common carriers by railroad, and only for the purpose of thereby affecting traffic rates for the transportation of persons and property." All such agreements, although their terms may be reasonable, and the rates established reasonable, are thus rendered invalid. It is sufficient if the necessary result of the agreement be the restraint of trade.[1] A monopoly in the manufacture of an article is not prohibited by this act.[2]

§ 179. **Contracts by trusts.**—As a general rule a contract made in violation of a statute is void, and when a party can not establish his cause of action without relying upon an illegal contract he can not recover. This doctrine has been invoked to prevent corporations which have entered into trust combinations from recovering on contracts made in aid of the object of the combination. In many states the anti-trust statutes provide that a purchaser of any article from any individual or corporation transacting business contrary to the provisions of the act shall not be liable for the price of the article, and may plead the act as a defense to an action for the purchase price. Where a corporation which was organized for the purpose of regulating the price of milk sold by its members to the dealers in a certain city, brought an action to recover for the value of milk sold to the defendant, it was held that the action was in furtherance of the illegal combination, and the plaintiff could not recover.[4] In another Illinois case

[1] For the present law relating to contracts in restraint of trade, see Diamond Match Co. v. Roeber, 106 N. Y. 473; Matthews v. Associated Press, 136 N. Y. 333; National Ben. Co. v. Union Hospital Co., 45 Minn. 272; Maxim-Nordenfelt, etc., Co. v. Nordenfelt, 2 The Reports 298 (1893), and same case in House of Lords; 11 The Reports 1 (1894). The entire subject is discussed with great learning by Lord Justices Bowen, Lindley and others.

[2] United States v. Knight, 156 U. S. 1.

[3] Ford v. Chicago, etc., Assn., 155 Ill. 166, reversing Chicago, etc., Assn. v. Ford, 46 Ill. App. 576.

it appeared that the defendant sold his property to a trust and transferred it by a bill of sale, but remained in possession as an employe for several years. He then repudiated the agreement, and took possession of his former property. The trust brought an action of replevin, and obtained judgment in its favor in the lower court, on the theory that the purchase of property by a foreign corporation in pursuance of a plan of monopoly does not prevent the title from passing.[1] This was reversed by the supreme court,[2] which said: "The bill of sale rests under the ban of the law, as well when executed to carry out the illegal agreement as if it had been made for the purpose of defrauding creditors. The law will not aid the appellee to recover the property, but will leave both it and the appellant where they were when the suit was begun." A somewhat different case is presented when it is sought to recover the value of property sold to the trust. Where the plaintiff (a brewing association) sold beer to a firm which was a member of a combination that was prohibited by statute, although not void at common law, the association was allowed to recover. The court said:[3] "The general rule, sustained by the great weight of authority, is to the effect that the buyer is not in a position to resist payment for goods bought by him for an unlawful purpose, known to the seller at the time of sale, unless it is made to appear that the seller has done something in furtherance of the unlawful act, besides the mere act of selling the goods with such knowledge." A corporation which appears to have been chartered in Illinois for an illegal purpose can enforce a stock subscription in New York, and the defendant will not be permitted to plead the illegal purpose of its organization.[4]

[1] Bishop v. American, etc., Co., 51 Ill. App. 417.

[2] Bishop v. American, etc., Co., 157 Ill. 284.

[3] Anheuser-Busch, etc., Co. v. Houck (Tex.), 27 S. W. Rep. 692. There are cases, however, which hold that the mere knowledge of the seller that the buyer will make illegal use of the goods will deprive him of the right to payment. See Hananer v. Doane, 12 Wall. (U. S.) 342.

[4] United States, etc., Co. v. Schlegel, 143 N. Y. 537. In National, etc., Co. v. Quick, 67 Fed. Rep. 130, it was held that a corporation organized for the purpose of securing assignments of all patents relating to spring tooth harrows, to grant licenses to the assignors to use the patents on the payment

§ 180. **Power to indorse and guarantee paper.**—Banking and manufacturing corporations have implied power to make negotiable paper for use within the scope of their corporate business, but not to become indorsers or guarantors for the accommodation of others.[1] No authority to lend its credit is implied from the mere fact that it may be beneficial to the corporation to do so. But if such paper passes into the hands of a bona fide holder without notice, it may be enforced.[2] So, if all the stockholders consent, an accommodation indorsement may be enforced.[3]

of royalties, to fix and regulate the prices at which the harrows shall be sold, and to take charge of all litigation and prosecute all infringements of such patents, is an illegal combination, and can not maintain a suit against a person who is infringing a patent.

[1] Blake v. Domestic Mfg. Co. (N. J. Ch.), 38 Atl. Rep. 241; Memphis, etc., Co. v. Memphis, etc., R. Co., 85 Tenn. 703, 5 S. W. Rep. 52; Tod v. Kentucky, etc., Co., 57 Fed. Rep. 47; Nat'l Bank of Republic v. Young, 41 N. J. Eq. 531; Nat'l Park Bank v. German, etc., Co., 116 N. Y. 281; Nat'l Bank v. Wells, 79 N. Y. 498; Ætna Nat'l Bank v. Charter Oak, etc., Co., 50 Conn. 167; Monument Nat'l Bank v. Globe Works, 101 Mass. 57; Davis v. Old Col. R. Co., 131 Mass. 258; Culver v. Reno R. Co., 91 Pa. St. 367; Webster v. Howe, etc., Co., 54 Conn. 394; Lucas v. White Line, etc., Co., 70 Iowa 541; Merchants' Nat'l Bank v. Detroit, etc., Works, 68 Mich. 620; Nat'l Bank v. Atkinson, 55 Fed. Rep. 465. A manufacturing corporation has no power to become a negotiator of bonds upon commission. Peck-Williamson, etc., Co. v. Oklahoma Board of Ed. (Okla.), 50 Pac. Rep. 236. In California a corporation may for a valuable consideration guarantee or assume the dept of another corporation. Smith v. Ferres, etc., R. Co., 51 Pac. Rep. 710. A guarantee by a brewing company of the payment of rent for a hotel in which its beer is sold is valid. Winterfield v. Cream City, etc., Co., 96 Wis. 239, 71 N. W. Rep. 101.

[2] In re Jacoby-Mickolas Co. (Minn.), 70 N. W. Rep. 1085; Jacobs Pharmacy Co. v. Southern, etc., Co., 97 Ga. 573, 25 S. E. Rep. 171; Farmers' Nat'l Bank v. Suton, etc., Co., 52 Fed. Rep. 191; Bank of Genesee v. Patchin Bank, 19 N. Y. 312; Nat'l Bank v. Young, 41 N. J. Eq. 531, 7 Atl. Rep. 488; Credit Co. v. Howe, etc., Co., 54 Conn. 357, 8 Atl. Rep. 472. See Holmes v. Willard, 125 N. Y. 75. Notes given for the obligations of the corporate officers are presumptively accommodation paper and *ultra vires*. Germania, etc., Co. v. Boynton, 71 Fed. Rep. 797, 19 C. C. A. 118; McLellan v. File Works, 56 Mich. 579.

[3] Martin v. Niagara, etc., Co., 122 N. Y. 165; Barr v. N. Y., etc., R. Co., 125 N. Y. 263; Thompson v. Lambert, 44 Iowa 239. In Mercantile Trust Co. v. Kiser, 91 Ga. 636, it was held that a sawmill corporation might, with the express consent of all the stockholders, guarantee the interest on the bonds of a railway, the construction of which was necessary to the successful prosecution of the business of the corporation.

Railway corporations are sometimes given express authority to guarantee bonds of other corporations. Power to guarantee such bonds upon such conditions and terms as may be agreed upon includes the power to receive as consideration for such guarantee stock of the company whose bonds are thus guaranteed. Where a corporation organized under the laws of Ohio for the purpose of making iron work for a mining plant attempted to guarantee the performance of another contract for the erection of a mining plant, it was claimed that the power existed on the ground that the guarantee would secure a sale of the iron work to be used in the plant. The court said that the general rule in this country and in England is that one corporation is impliedly prohibited from guaranteeing the contract or debt of another, on the ground that such a guarantee exposed the funds of the company to the risk of a different enterprise and business under the control of different persons than those which its stockholders, creditors and the state had a right from its charter to expect.[1] But it was held that under articles of incorporation which provide that the corporation may do all things proper and necessary to carry on the lumber business, the corporation may become a surety on the bonds of building contractors when it appeared that such was the custom among lumber companies.[2] A guarantee may thus sometimes be lawfully made for the purpose of carrying out the purposes of the corporation. When a railroad corporation has received the bonds of a municipal corporation in payment for its stock, it may, in order to sell them, guarantee their payment.[3] A provision that the articles of incorporation shall state the purposes for which it is formed and that it shall not be lawful for it to direct its operations or appropriate its funds to any other purpose, is for the protection of the public, and does not operate on the contracts of the corporation so as to prevent it from recovering on a mortgage given to indemnify it

[1] Humboldt, etc., Co. v. American, etc., Co., 62 Fed. Rep. 357, 10 C. C. A. 415.

[2] Wheeler v. Everett, etc., Co., 14 Wash. 639, 45 Pac. Rep. 316.

[3] Chicago, etc., R. Co. v. Howard, 7 Wall. (U. S.) 392; Low v. Railway Co., 52 Cal. 53.

for guaranteeing the payment of the notes of another corporation, after it has paid such notes.[1] A corporation may indorse paper which it holds for the purpose of negotiating it.[2] The guaranty by a railroad company of the bonds of a connecting road, made under power given by its charter for the purpose of securing valuable business connections, is not a fundamental business change and may therefore be exercised by the board of directors.[3]

§ 181. **To enter into a partnership.**—Corporations generally have no power to enter into a partnership with individuals or other corporations, or into agreements which may create partnerships.[4] This rule applies with particular force when the business to be conducted by the partnership is *ultra vires* the corporation.[5] A combination or syndicate formed by five corporations engaged in manufacturing cotton-seed oil, under an agreement by which all the plants were placed in the hands and under the management and control of a committee composed of representatives from each corporation, each corporation to share in the profit or loss, was held to be a partnership, and the agreement invalid.[6]

§ 182. **To borrow money and make negotiable paper.**—A corporation has implied power to raise money for purposes properly within the scope of its business. It may, of course, for this purpose issue and sell its stock within the limit allowed by law and may even issue preferred stock in order to more readily find purchasers. It also has implied power to borrow

[1] Butterworth v. Kritzer Mill Co. (Mich.), 72 N. W. Rep. 990; Union Nat'l Bank v. Matthews, 98 U. S. 621; McIndoe v. St. Louis, 10 Mo. 575.

[2] Bank v. Patchin Bank, 13 N. Y. 309.

[3] Louisville Trust Co. v. Louisville, etc., Co., 75 Fed. Rep. 433.

[4] Oscillating Carousal Co. v. McCool (N. J. Ch.), 35 Atl. Rep. 585; People v. North River, etc., Co., 121 N. Y. 582; Mallory v. Oil Works, 86 Tenn. 598; Marine Bank v. Ogden, 29 Ill. 248. See French v. Donahue, 29 Minn. 111; Allen v. Woonsocket Co., 11 R. I. 288.

[5] Whittenton Mills v. Upton, 10 Gray (Mass.) 582; Central, etc., Co. v. Smith, 76 Ala. 572; Standard Oil Co. v. Scofield, 16 Abb. (N. C.) 372. See Bates v. Coronado Beach Co., 109 Cal. 160.

[6] Gunn v. Central R. Co., 74 Ga. 509.

money to enable it to carry out its legitimate objects and to execute the ordinary commercial paper involved in such transaction. The weight of modern authority supports the conclusion that private corporations organized for pecuniary profit may, like individuals, borrow money whenever the nature of their business renders it proper or expedient that they should do so, subject only to such express limitations as are imposed by their charters. The power to borrow carries with it by implication, unless restrained by the charter, the power to secure the loan by mortgage. It may, therefore, be regarded as settled that, when general authority is given to engage in business and there are no special restraints in its charter, it takes the power as a natural person enjoys it, with all its incidents and accessories. It may borrow money to attain its legitimate objects, precisely as an individual, and bind itself by any form of obligation not forbidden.[1]

The power to borrow money is implied from an expressed power to do an act which requires the use of money. Thus a corporation which under a statute may "hold real and personal estate, and may hire, purchase or erect suitable buildings for its accommodations to an amount not exceeding five hundred thousand dollars," may take a lease of land and erect a building thereon and borrow the money necessary for such purpose.[2]

[1] Wright v. Hughes, 119 Ind. 324; Jones v. Guaranty Co., 101 U. S. 622; Reichwald v. Hotel Co., 106 Ill. 439; Booth v. Robinson, 55 Md. 419; Hayes v. Coal Co., 29 Ohio St. 330; Railroad Co. v. Dow, 19 Fed. Rep. 388; Curtiss v. Leavitt, 15 N. Y. 9; Kent v. Quicksilver, etc., Co., 78 N. Y. 159; Ward v. Johnson, 95 Ill. 215; Commissioners v. Ry. Co., 77 N. C. 289; Fifth Ward Sav. Bank v. First Nat'l Bank, 48 N. J. Law 513; In re Durham County, etc., Soc., Lower Courts, 12 Eq. 516; Kneeland v. Braintree, etc., R. Co., 167 Mass. 161, 45 N. E. Rep. 86. The president and secretary of a corporation have no inherent power to execute negotiable notes in the name of the corporation. City, etc., R. Co. v. Bank, 62 Ark. 33, 31 L. R. A. 535.

[2] Bradbury v. Boston Canoe Club, 153 Mass. 77; Davis v. Old Colony R. Co., 131 Mass. 258. The right of a building and loan society to execute negotiable paper is implied from power to incur debts for various purposes, and to sell and mortgage property. Grommes v. Sullivan, 53 U. S. App. 359, 81 Fed. Rep. 45, reversing Towle v. Am., etc., Co., 78 Fed. Rep. 688. See note to 43 L. R. A. 419, on power of building associations to issue negotiable paper.

Such power is plainly inferable from a charter limitation upon the amount of the indebtedness.[1]

If the execution of negotiable paper is obviously foreign to the purposes of the corporation all persons are chargeable with notice of the *ultra vires* character of such paper. But if the business of the corporation is such that it may under some conditions have occasion to execute such paper, and it in fact executes it for a purpose foreign to its purposes, as in payment for property which it had no authority to purchase, the paper is binding in the hands of a bona fide holder for value without notice. The distinction is between a total want of power and an irregular exercise of an unauthorized power.[2]

§ 183. **Limitations upon the amount of indebtedness.**—A person dealing with a corporation is charged with notice of its powers as disclosed by the charter or articles of incorporation.[3]

[1] Auerbach v. LeSueur, etc., Co., 28 Minn. 291. Some earlier decisions show an inclination to restrict this power. Thus, in Bateman v. Mid-Wales Ry. Co., Lower Courts, 1 C. P. 499 (1866), it was held that a railway company, with a limited capital and a limited power of borrowing money, had no power to accept bills. But in Union Bank v. Jacobs, 6 Humph. (Tenn.) 515 (1845), where it was contended that the money paid for capital stock was the only means provided by which to raise money to pay a debt, the court said: "The restriction contended for is too refined and technical. It might have suited the days of the year books, when it was held that a corporation could contract for nothing except under its corporate seal; but it is strange that it should be urged at this day of enlightened jurisprudence, when the substance of things is looked to rather than forms. A corporation is, in the estimation of the law, a body created for special purposes, and there is no good reason why it should not, in the execution of these purposes, resort to any means that would be necessary and proper for an individual in executing the same, unless it be prohibited by the terms of its charter or some published law from so doing.

"There is no principle which prevents a corporation from contracting debts within the scope of its action; and, as has been observed, if it may contract a debt, it necessarily may make provision for its payment by drawing, or indorsing, or accepting notes or bills. It is not pretended that this power extends to the drawing, indorsing or accepting bills or notes generally, and disconnected with the purposes for which the corporation was created."

[2] Monument Nat'l Bank v. Globe Works, 101 Mass. 57; Nat'l Park Bank v. German, etc., Co., 116 N. Y. 281; Nat'l Bank v. Young, 41 N. J. Eq. 531; Jacob's, etc., Co. v. Southern, etc., Co., 97 Ga. 573, 25 S.E. Rep. 171; Bradley v. Ballard, 55 Ill. 413.

[3] Pearce v. Madison, etc., R. Co., 21

Hence, when the amount of indebtedness which may be incurred is limited by the charter, one who loans it an amount in excess of the limit, can not recover the excess. If, however, there is no bad faith and the contract is not against public policy, the contract is valid to the limit of indebtedness. With reference to the apparently conflicting authorities, Mr. Justice Mitchell said:[1] "They all fall within one or the other of three classes: (1) Where the act was not in violation of the company's charter, but was merely claimed to be in excess of the powers delegated to some inferior agent; or (2) where the corporation had received and retained the benefits of the transaction; or (3) where the fact that the power of the corporation in that regard had been exhausted depended on the existence of certain extrinsic facts not known to the other contracting party.[2] Dicta may be found in a few cases to the effect that limitations like this upon the amount of indebtedness which the corporation can contract are merely directory. But there can be no distinction in principle between a case where the charter or articles of association prohibit a thing altogether, and where it is prohibited beyond a certain limit. In the one case, there is a total absence of authority to do the thing at all, and in the other a total absence of authority to do it beyond a certain limit; and after that limit is reached there is as much an absence of authority in the latter case as there is in the former. No other rule would keep corporations in subordination to the state or properly protect shareholders, for whose special benefit

How. (U. S.) 441; Davis v. Old Colony R. Co., 131 Mass. 258; Fitzhugh v. Land Co., 81 Tex. 306.

[1] Kraniger v. People's Building Soc., 60 Minn. 94; Oswald v. Times Printing Co., 65 Minn. 219. As to what are debts, see Lockhart v. Van Alstyne, 31 Mich. 76; Chase v. Curtis, 113 U. S. 452; Leighton v. Campbell, 17 R. I. 51; Childs v. Boston, etc., Works, 137 Mass. 516.

[2] If a person loans money to the corporation, in ignorance that the limit has been reached, he can recover. Humphrey v. Patrons', etc., Assn., 50 Iowa 607; Ossipee Mfg. Co. v. Canney, 54 N. H. 295; Conn. River Sav. Bank v. Fiske, 60 N. H. 363. The person who loans money to the corporation is affected by notice when his loan exceeds the charter limitation. First Nat'l Bank v. Kiefer, 95 Ky. 97. As to what is included in "indebtedness," see Tradesman's Pub. Co. v. Knoxville, etc., Co., 95 Tenn. 634, 31 L. R. A. 593.

the limitations, whether self-imposed or imposed by statute, are usually intended."

§ 184. **Liability to holder of over-issued negotiable paper.** Where the charter of a trading corporation provided that "the highest amount of indebtedness or liability to which said corporation shall be subject shall not exceed five thousand dollars," and the corporation, nevertheless, contracted indebtedness and gave its promissory notes for a greater amount, it was held that a bona fide purchaser of the paper before maturity could recover thereon from the corporation. The court said:[1] "Where a private corporation has authority to issue negotiable securities, such instruments when issued possessed the legal character ordinarily attaching to negotiable paper, and the holder in good faith before maturity and for value may recover, even though in a particular case the power of the corporation was irregularly exercised or was exceeded; or, to state the legal proposition in its application to this case, this defendant having power to incur debts to a limited extent and to issue its negotiable notes therefor, the plaintiff, as a bona fide holder of the note in suit, may recover upon it, although in this particular case the indebtedness of the corporation at the time of giving this note already exceeded the limits prescribed by its articles of association. Although, in such a case, the corporation or its officers exceeded the corporate authority, and its contract would be, hence, in a sense *ultra vires*, yet other legal principles besides those merely relating to the powers of a corporation come in to affect the result."

A limitation of the indebtedness to an amount equal to one-half of the capital stock of the corporation means one-half of the paid-up capital stock.[2]

[1] Auerbach v. LeSueur, etc., Co., 28 Minn. 291-296; Stoney v. American, etc., Co., 11 Paige (N. Y.) 635; Monument Nat'l Bank v. Globe Works, 101 Mass. 57; Bissell v. Michigan, etc., R. Co., 22 N. Y. 258-289; City of Lexington v. Butler, 14 Wallace (U. S.) 282; Ossipee Mfg. Co. v. Canney, 54 N. H. 295; Garrett v. Burlington, etc., Co., 70 Iowa 697.

[2] Appeal of Lehigh, etc., R. Co., 129 Pa. St. 405.

§ 185. **Power to acquire personal property.**—The power to acquire real property by purchase or devise has already been considered.[1] The common law placed no limit on the quantity or value of personal property which a corporation might acquire, although, from the nature of the business of the corporation, it might be inferentially prohibited from investing its funds in certain kinds of personal property. The limitation in such cases is upon the power to acquire the particular kind of property and not upon the power to acquire property. The statutes of mortmain had no application to personal property, and a corporation always had the power to take personal property by bequest.[2]

§ 186. **Power of alienation.**—Independent of positive law, all corporations have the absolute *jus disponendi*, neither limited as to objects nor circumscribed as to quantity.[3] One of the earliest writers on the law of corporations stated the common law rule to be that all civil corporations, unless expressly restrained by the act which established them, or by some subsequent act, have and always have had an unlimited control over their respective properties, and may alienate in fee or make what estates they please, for years, for life, or in tail, as fully as any individual may do with respect to his own property.[4] When thought desirable, a corporation having no public duties to perform may dispose of all its property and wind up its business. Hence, the directors of a corporation which has been unsuccessfully carrying on the business for which it was organized may, with the consent of the majority of the stockholders, validly lease the plant of the corporation to another corporation carrying on the same business, even though a minority of the stockholders object thereto.[5]

[1] § 160, *et seq.*, *supra*. Stockton, etc., v. Staples, 98 Cal. 189; Nicoll v. New York, etc., Co., 12 N. Y. 121.

[2] Sherwood v. American, etc., Soc., 4 Abb. (N. Y. Ct. App. Cas.) 231.

[3] Kent Com., Vol. II, p. 280; 7 Eng. Rul. Cas. 377, note; Wood v. Bedford, etc., R. Co., 8 Phila. 91; Angell & Ames Corps., § 191; Hendee v. Pinkerton, 14 Allen (Mass.) 381; Dupee v. Water, etc., Co., 114 Mass. 37; Benbow v. Cook, 115 N.C. 324; Wythe, etc., Co. v. James, etc., Co., 15 Utah 110.

[4] Kyd Corp. (1st ed., 1793), 107, 108; Aurora Society v. Paddock, 80 Ill. 264.

[5] Bartholomew v. Derby, etc., Co.,

§ 187. **Limitations upon the right of alienation—Corporations charged with public duties.**—The general rule that a corporation may alienate its property with the same freedom as an individual is subject to the limitation that a corporation charged with duties to the public, and which has received its franchises and privileges from the state in consideration of the assumption and performance of such duties, can not sell or dispose of its franchises or of the property which is essential to the performance of such duties without authority from the state.[1] This rule also restricts the power to mortgage such property, as the execution of a valid mortgage necessarily contemplates a possible if not a present change of title. Upon the same rule of public policy rests the principle that "land which has been appropriated to corporate objects, and is necessary for the full enjoyment and exercise of any franchise of the company, whether acquired by a purchase or by exercise of the delegated power of eminent domain," is held exempt from levy or sale. This "on no ground of prerogative or corporate immunity, for the company can no more alien or transfer such lands by their own act than can a creditor by legal process; but the exemption rests on the public interests involved in the corporation." But the reason for the rule fails when a corporation owns land for other than corporate purposes. Hence, lands held for other purposes, and not actually dedicated to corporate uses, may be levied on and sold in the same manner as the lands of any other debtor.[2] A manufacturing corporation has the right to lease or rent its plant temporarily when the purpose is not the abandonment of its franchise, but the raising of a fund to enable it thereafter to transact its business more profitably.[3]

§ 188. **Power to give a mortgage.**—As a general rule a corporation may mortgage the property it holds for corporate

69 Conn. 521. As to powers of the majority, see further, § 485.

[1] City, etc., Co. v. State, 88 Tex. 600, 32 S. W. Rep. 1033; Central, etc., Co. v. Pullman, etc., Co., 139 U. S. 24; Oregon R. Co. v. Oregonian R. Co., 130 U. S. 1; Pennsylvania R. Co. v. St. Louis, etc., R. Co., 118 U. S. 290.

[2] Plymouth R. Co. v. Colwell, 39 Pa. St. 337.

[3] Plant v. Macon, etc., Co., 103 Ga. 666, 30 S. E. Rep. 567.

purposes, unless expressly prohibited from doing so.[1] The power may be implied from the power to borrow money[2] or from the power to take and hold real estate and make contracts[3] or from power "to acquire, alien, transfer and dispose of property of every kind."[4] The limitation upon the general rule which forbids corporations charged with public duties to sell or mortgage their franchises or the property which is essential to the performance of such duties has already been stated.[5] Under such circumstances, the corporation has no power to mortgage such property or franchises without express authority; but a corporation which is authorized to sell its franchises is authorized to mortgage them, as a mortgage is in effect a sale with a power of defeasance which may ultimately end in an absolute transfer of title.[6] It has been held that under the New York statute a manufacturing corporation can mortgage property for the purpose of securing a debt but not to raise money,[7] although this ruling has been considerably limited.[8]

A corporation can not make a valid mortgage upon its future income without express legislative authority under a statute

[1] England v. Dearborn, 141 Mass. 590; State v. Rice, 65 Ala. 83; Watts Appeal, 78 Pa. St. 370; Phillips v. Winslow, 18 B. Mon. (Ky.) 431, 68 Am. Dec. 729; Warfield v. Marshall Co., 72 Iowa 666, 2 Am. St. Rep. 263; Love v. Siera, etc., Co., 32 Cal. 639, 91 Am. Dec. 602; In re Pat. File Co., L. R. 6 Ch. App. 83, 7 Eng. Rul. Cas. 668.

[2] Wright v. Hughes, 119 Ind. 324, 12 Am. St. Rep. 412; Fitch v. Steam Mill Co., 80 Me. 34; Lehigh Valley, etc., Co. v. Agricultural Works, 63 Wis. 45; Barry v. Exchange Co., 1 Sandf. Ch. (N. Y.) 280; Curtis v. Leavitt, 15 N. Y. 9; Eureka, etc., Works v. Bresnahan, 60 Mich. 332; Reichwald v. Hotel Co., 106 Ill. 439; Evans v. Heating Co., 157 Mass. 37; Jones v. Indemnity Co., 101 U. S. 622.

[3] Watts Appeal, 78 Pa. St. 370; Aurora, etc., Soc. v. Paddock, 80 Ill. 263.

[4] McAllister v. Plant, 54 Miss. 106.

[5] § 186. Thomas v. Railroad Co., 101 U. S. 71; Commonwealth v. Smith, 10 Allen (Mass.) 448, 87 Am. Dec. 672; Lord v. Gas Co., 99 N. Y. 547; Carpenter v. Mining Co., 65 N. Y. 43; Daniels v. Hart, 118 Mass. 543; City Water Co. v. State, 88 Tex. 600; Bank v. Delaware, etc., Co., 22 N. J. Eq. 130; Pierce v. Emery, 32 N. H. 484. *Contra*: Shepley v. Railroad Co., 55 Maine 395; Bardstown R. Co. v. Metcalf, 4 Metc. (Ky.) 199, 81 Am. Dec. 541; Bank v. Edgerton, 30 Vt. 182; Kennebec, etc., R. Co. v. Portland, etc., R. Co., 59 Maine 9.

[6] Williamette Mfg. Co. v. Bank of Columbia, 119 U. S. 191; Commonwealth v. Smith, 10 Allen (Mass.) 448.

[7] Carpenter v. Black Hawk Mfg. Co., 65 N. Y. 43.

[8] Lord v. Yonkers, etc., Co., 99 N. Y. 547.

which forbids a mortgage of property which may be acquired after the execution of the mortgage.[1] A mortgage given to secure money borrowed in excess of the amount allowed by the statute is valid as against subsequent creditors who became such with knowledge of all the facts.[2] A corporation can not contest the validity of an agreement by which another corporation undertook to subject its property to a mortgage executed by the former corporation for the purpose of securing bonds, on the ground that the agreement is *ultra vires*.[3]

§ 189 **Assignment for benefit of creditors.—Preferences.—** A corporation, when not forbidden by statute, may make an assignment for the benefit of its creditors.[4] As said by one court,[5] "the weight of authority seems to be in favor of the proposition that the board of directors of a corporation, to which the general management of its affairs is committed without particular restriction, may authorize a general assignment of the corporate property for the benefit of creditors, when the condition of affairs is such as to reasonably justify such a course, as in the case of insolvency."

So, by the weight of authority, in the absence of a prohibitive statute, an insolvent corporation may deal with its property in the same manner as an individual, and may, therefore, make an assignment with preferences in favor of certain creditors.[6]

[1] Lubroline Oil Co. v. Athens Sav. Bank (Ga.), 30 S. E. Rep. 409.

[2] Central Trust Co. v. Columbus, etc., R. Co., 87 Fed. Rep. 815.

[3] The Illinois, etc., Bank v. Pacific R. Co., 115 Cal. 287, 49 Pac. 196.

[4] Ardesco Co. v. North American, etc., Co., 66 Pa. St. 375; State v. Bank, etc., 6 Gil. & J. 206; Shockley v. Fisher, 75 Mo. 498; Fouche v. Brower, 74 Ga. 251; Reichwald v. Hotel Co., 106 Ill. 439; Glover v. Lee, 140 Ill. 102; Tripp v. N.W. Nat'l Bank, 41 Minn. 400; Chase v. Tuttle, 55 Conn. 455; Coats v. Donnell, 94 N. Y. 168; Lamb v. Cecil, 25 W. Va. 288; Chamberlain v. Bromberg, 83 Ala. 576; Rollins v. Carriage Co., 80 Iowa 380; Bank, etc., v. Potts, etc., Co., 90 Mich. 345; Boynton v. Roe (Mich.), 72 N. W. Rep. 257.

[5] Tripp v. N.W. Nat'l Bank, 41 Minn. 400. The directors may make the assignment without the assent of the stockholders. Boynton v. Roe (Mich.), 72 N. W. Rep. 257; Hutchinson v. Green, 91 Mo. 367; DeCamp v. Alward, 52 Ind. 473.

[6] Brown v. Grand Rapids, etc., Co. (U. S. C. C. App.), 58 Fed. Rep. 286, 22 L. R. A. 817; Catlin v. Eagle Bank, 6 Conn. 233; Gould v. Little Rock, etc., R. Co., 52 Fed. Rep. 680; Ringo v. Biscoe, 13 Ark. 563; Bank v. Whittle, 78 Va. 737; Buell v. Buckingham, 16 Iowa

This rule is generally criticised by text writers,[1] but without much apparent result. Some decisions hold that as the property of an insolvent corporation is a trust fund, held by the corporation for the benefit of all its creditors, it can not be disposed of by way of a preference.[2] The rule has every reason in its favor and has been embodied in the statutes of some states.[3] But, as said by Judge Caldwell,[4] although "a

284, 85 Am. Dec. 516; Warfield v. Marshall, etc., Co., 72 Iowa 666; Rollins v. Shaver, etc., Co., 80 Iowa 380; Allis v. Jones (Neb.), 45 Fed. Rep. 148; Henderson v. Indiana, etc., Co., 143 Ind. 561; Vail v. Jameson, 41 N. J. Eq. 648; Wilkinson v. Bauerle, 41 N. J. Eq. 635; Pyles v. Riverside, etc., Co., 30 W. Va. 123; San Diego, etc., Co. v. Pacific, etc., Co., 112 Cal. 53, 33 L. R. A. 788; Bank, etc., v. Potts, etc., Co., 90 Mich. 345; Haywood v. Lincoln, etc., Co., 64 Wis. 639; Glover v. Lee, 140 Ill. 102; Illinois, etc., Co. v. O'Donnell, 156 Ill. 624, 31 L. R. A. 265; Butler v. Robbins Co., 151 Ill. 588; Union Nat'l Bank v. State Nat'l Bank, 168 Ill. 256, 48 N. E. Rep. 82; Sells v. Grocery Co., 72 Miss. 590; Alberger v. Bank, 123 Mo. 313; Schufeldt v. Smith, 131 Mo. 280; Sanford, etc., Co. v. Howe, 157 U. S. 312; Smith v. Skeary, 47 Conn. 47; Coats v. Donnell, 94 N. Y. 168. See the dissenting opinion by Kellam, J., in Adams & Westlake Co. v. Deyette (S. Dak.), 65 N. W. Rep. 471.

[1] Thompson Corp., § 6493, *et seq.* Taylor Corp., § 668; Morawetz Corp., § 803; Wait Insolvent Corp., § 162.

[2] Rouse v. Merchants' Nat'l Bank, 46 Ohio St. 493, 5 L. R. A. 378; Brown v. Morristown, etc., Co. (Tenn. Ch. App.), 42 S. W. Rep. 161; Lyon-Thomas H. Co. v. Perry, etc., Co., 86 Tex. 143, 22 L. R. A. 802, Ann.; Thompson v. Lumber Co., 4 Wash. 600; Haywood v. Lincoln, etc., Co., 64 Wis. 639. In Wisconsin a statute makes all preferences except for wages void. Ford v. Bank, 87 Wis. 363; Adams, etc., Co. v. Deyette, 8 S. Dak. 119; Biddle, etc., Co. v. Steel Co., 16 Wash. 681; Tradesman's, etc., Co. v. Wheel Co., 95 Tenn. 634; Swepson v. Bank, 9 Lea. (Tenn.) 713. The president and general manager of a corporation, although having entire charge of its affairs, can not in the absence of special authority transfer its assets after insolvency to one of its creditors so as to give him a preference. Hadden v. Linville (Md.), 38 Atl. Rep. 37; Kankakee, etc., Co. v. Kampe, 38 Mo. App. 229, (to a director) 5. In a case arising in Ohio, the supreme court of the United States followed the decision in Rouse v. Merchants' Nat'l Bank, *supra*; Smith, etc., Co. v. McGroarty, 136 U. S. 237.

[3] See Throop v. Lithographing Co., 125 N. Y. 530; Scott v. Armstrong, 146 U. S. 499; Varnum v. Hart, 119 N. Y. 101. See French v. Andrews, 145 N. Y. 441, U. S. Rev. St., § 5242; Irons v. Mfg. Bank, 6 Biss. (C. C.) 301. Certain statutory preferences are also commonly authorized to clerks, servants, employes, etc. See Lewis v. Fisher, 80 Md. 139, 26 L. R. A. 278; Palmer v. Van Santvoord, 153 N. Y. 612, 38 L. R. A. 402; Boston, etc., Co. v. Mercantile, etc., Co., 82 Md. 536, 38 L. R. A. 97, for construction of such statute.

[4] Gould v. Railway Co., 52 Fed. Rep. 680, 684.

good many courts have, from time to time, inveighed against the rule of the common law which allows a debtor to make preferences among his creditors, the rule is too firmly imbedded in our system of jurisprudence to be overthrown by judicial decision, and it can no more be overthrown by the courts in its application to corporations than to individuals." After quoting the statement: "Both reason and authority establish the proposition that a corporation may sell and transfer its property, and may prefer its creditors, although it is insolvent, unless such conduct is prohibited by law,"[1] the court continued:[2] "We think this is a correct statement of the rule, and that it can only be abrogated by legislation." When preferences are allowed, a stockholder who is a bona fide creditor may be preferred.[3] But a director stands in a trust relation to the stockholders and, after insolvency, to the creditors of the corporation. The better rule would seem to be that an insolvent corporation can not prefer a director or managing agent,[4] although there are decisions to the effect that a director who is a bona fide creditor may be preferred.[5]

[1] Wilkinson v. Bauerle, 41 N. J. Eq. 635.

[2] Gould v. Little Rock, etc., R. Co., 52 Fed. Rep. 680.

[3] Reichwald v. Com., etc., Co., 106 Ill. 439; Lexington, etc., Co. v. Page, 17 B. Mon. (Ky.) 416, 66 Am. Dec. 165.

[4] Olney v. Conanicut Land Co., 16 R. I. 597, 5 L. R. A. 361; Consol. Tank Line v. Kansas City, etc., Co., 45 Fed. Rep. 7; Hays v. Citizens' Bank, 51 Kan. 535; Smith v. Putnam, 61 N. H. 632; Corey v. Wadsworth, 99 Ala. 68, 23 L. R. A. 618; Lyon, etc., Co. v. Perry, etc., Co. (Tex.), 22 L. R. A. 802, Ann. In Howe, etc., Co. v. Sanford, etc., Co., 44 Fed. Rep. 231, the court said: "It seems to me enough to say that a sound public policy and a sense of common fairness forbids that the directors or managing agents of a business corporation, when disaster has befallen or threatens the enterprise, shall be permitted to convert their powers of management and their intimate and may be exclusive knowledge of the corporate affairs into means of self-protection, to the harm of other creditors." Seeds, etc., Co. v. Heyn, etc., Co. (Neb.), 77 N. W. Rep. 660; Hill v. Pioneer, etc., Co., 113 N. C. 173, 21 L. R. A. 560.

[5] Planters' Bank v. Whittle, 78 Va. 737; Schufeldt v. Smith, 131 Mo. 280, 29 L. R. A. 830; Buell v. Buckingham, 16 Iowa 284, 85 Am. Dec. 516; South Bend, etc., Co. v. Cribb Co. (Wis.), 72 N. W. Rep. 749; Bank of Montreal v. Potts, etc., Co., 90 Mich. 345. In Brown v. Grand Rapids, etc., Co. (C. C. App.), 22 L. R. A. 817, 58 Fed. Rep. 286, Judge Taft said: "All the decisions of the supreme court of the United States relied on and referred to as sustaining the view that

An assignment by a corporation for the benefit of its creditors is not invalidated by the preference of the claim of a banking corporation, of which one of the directors of the insolvent corporation is president, director, and a large stockholder, when it was approved by the unanimous vote of the stockholders and directors of the corporation. The assignment was made in good faith, without fraud, in fact.[1] So, a preference may be given to a creditor whose notes are guaranteed by its directors.[2]

§ 190. **Power to hold stock in another corporation.**—As a general rule it may be stated that a corporation can not purchase, hold, or deal in the stock of other corporations without express or implied authority so to do.[3] The power may, however, arise by implication, and may, therefore, be exercised when

the bona fide debt of a director of a corporation may not be paid in preference to the debt of some other creditor are cases where the directors were guilty of fraud in procuring the payment of their own debts by fraudulent wasting of the assets to accomplish the preference. Such were the cases of Drury v. Milwaukee, etc., R. Co., 7 Wall. 299; Koehler v. Black River, etc., Co., 2 Black. 715; Jackson v. Ludeling, 21 Wall. 616." The fact that the creditor is related to one or more of the directors or officers will not prevent the giving of a valid security as a preference to such creditor. Blair v. Ill., etc., Co., 159 Ill. 350, 31 L. R. A. 269.

[1] Colorado Fuel, etc., Co. v. Western, etc., Co. (Utah), 50 Pac. Rep. 628, distinguishing Sutton Mfg. Co. v. Hutchinson, 63 Fed. Rep. 496, 24 U. S. App. 145; Haywood v. Lincoln, etc., Co., 64 Wis. 639.

[2] Blair v. Ill., etc., Co., 159 Ill. 350, 31 L. R. A. 269.

[3] People v. Chicago, etc., Co., 130 Ill. 268, 17 Am. St. Rep. 319; Franklin Co. v. Lewiston Sav. Inst., 68 Maine 43; Franklin Bank v. Commercial Bank, 36 Ohio St. 350; People v. Pullman, etc., Co., 175 Ill. 126; Milbank v. Railway Co., 64 How. Pr. (N. Y.) 320; Nassau Bank v. Jones, 95 N. Y. 115; Pearson v. Concord, etc., Co., 62 N. H. 537; Oregon, etc., R. Co. v. Oregonian, etc., Co., 130 U. S. 1; Valley, etc., R. Co. v. Lake Erie, etc., Co., 46 Ohio St. 44; Central, etc., R. Co. v. Penn., etc., R. Co., 31 N. J. Eq. 475; Byrnes v. Mfg Co., 65 Conn. 365, 28 L. R. A. 304; Denny, etc., Co. v. Schram, 6 Wash. 134, 36 Am. St. Rep. 130; Marble Co. v. Harvey, 92 Tenn. 115; Knowles v. Sandersock, 107 Cal. 629; Easun v. Buckeye Co., 51 Fed. Rep. 156. In Farmers' Loan and Trust v. New York, etc., R. Co., 150 N. Y. 410, 34 L. R. A. 76, it was held that the statutory right of a corporation to purchase the stock of another company does not give the right, as the owner of a majority of the stock and bonds of the company, to so manage its affairs as to cause a default on a mortgage, and thus obtain control of the property by a foreclosure at less than its value, to the detriment of minority stockholders. See De La Vergne, etc., Co. v. German, etc., Inst. (U. S. S. Ct.), 19 Nat. Corp. L. Rep. 542.

necessary to the exercise of its granted powers, or when reasonably necessary in order to carry out the objects of the corporation. If one corporation could purchase and hold the stock of another it could thus control the business of the latter corporation, and indirectly engage in a business, and thus exercise powers not granted or contemplated by its own charter. A contract by a railroad corporation to purchase shares in another such corporation for the purpose of obtaining control and thus preventing competition between the two is *ultra vires* and illegal.[1] Where one gas company purchased stock of another, the court said:[2] "Where a charter in express terms confers upon a corporation the power to maintain and operate works for the manufacture and sale of gas, it is not a necessary implication therefrom that the power to purchase stock in other gas companies should also exist. There is no necessary connection between manufacturing gas and buying stocks. * * * It is true that a gas company might take the stock of another company in payment of a debt, or perhaps as security for a debt, but the actual purchase of such stock is not directly and immediately appropriate to the execution of a specifically granted power to operate gas-works and manufacture gas. Some corporations, like insurance companies, may find it necessary to keep funds on hand for the payment of losses by death or fire, or to meet other necessary demands; but it is questionable whether they can invest their surplus funds in the stocks of other corporations without special legislative authority. * * * If, then, the power to purchase outside stocks can not be implied from the power to operate gas-works and make and sell gas, a company to which the latter power has been expressly granted can not exercise the former without legislative authority to do so. This is the law as settled by the great weight of authority." Corporations whose business it is to loan money may take stock in other corporations as collateral, and in the process of realizing on

[1] Central, etc., Co. v. Cullen, 40 Ga. 582; Pearson v. Concord, etc., R. Co., 62 N. H. 537.

[2] People v. Chicago, etc., Co., 130 Ill. 268.

the security, become the owner of the stock.[1] The general rule above stated, is subject to the exception that one corporation may acquire the shares of another when necessary to secure the payment of a debt,[2] although it may be expressly forbidden to purchase such stock.[3] So, the application of the rule is sometimes limited by the doctrine of estoppel. It is thus held that the objection that the purchase by a corporation of the stock of another corporation is *ultra vires*, can not be raised by the stockholders of the corporation whose stock is thus purchased.[4] But, in the United States courts, a corporation which unlawfully purchases stock in another corporation may, under all circumstances, assert the *ultra vires* character of the transaction.[5]

§ 191. **Exceptions to the general rule.**—In some states[6] and in England,[7] it is held that a corporation has implied power to purchase and hold the stock of another corporation. So, in many cases, the authority is expressly conferred,[8] while in others it is implied, from the express grant of power. Thus, the power to acquire stock in another corporation may be implied from authority to consolidate with such corporation.[9] A banking corporation with authority to "discount bills, notes and other securities," may purchase stock in another corporation.[10] A corporation may be formed for the purpose of dealing in bonds and stocks.[11] In some states it is

[1] First Nat'l Bank v. Nat'l Exchange Bank, 92 U. S. 122. See In re Asiatic Banking Corp., L. R. 4 Ch. App. 252.

[2] Howe v. Boston, etc., Co., 16 Gray (Mass.) 493.

[3] Holmes, etc., Co. v. Holmes, 127 U. S. 252.

[4] Kennedy v. Cal. Sav. Bank, 101 Cal. 495. Reversed in 167 U. S. 162, on grounds not affecting this proposition.

[5] California Bank v. Kennedy, 167 U. S. 362.

[6] See Iowa Lumber Co. v. Foster, 49 Iowa 25; Calumet Paper Co. v. Statts' Ins. Co., 96 Iowa 147, 64 N. W. Rep. 782; Booth v. Robinson, 55 Md. 419; Hill v. Nisbet, 100 Ind. 341; Evans v. Bailey, 66 Cal. 112.

[7] In re Asiatic Banking Corp., L. R. 4 Ch. App. 252; In re Barned's Banking Co., L. R. 3 Ch. App. 105.

[8] Minn. Gen. St. 1894, § 2834, construed in Cowling v. Zenith Iron Co., 65 Minn. 263, 33 L. R. A. 508.

[9] Louisville, etc., Co v. Louisville, etc., R. Co., 75 Fed. Rep. 433.

[10] Latimer v. Citizens' State Bank, 102 Iowa 161, 71 N. W. Rep. 225.

[11] Market St. R. Co. v. Hellman, 109 Cal. 571.

held that a purely private corporation, owing no duties to the public may, when necessary to make an advantageous sale of its property, sell the same to another corporation and take its stock in payment therefor.[1] In all cases a corporation may take the stock of another corporation for the purpose of securing payment of an existing indebtedness.[2] And it may acquire title to stock in another corporation by levying on the same and selling it under execution to satisfy a judgment against the corporation.[3] For the purpose of retiring from business, a corporation may sell the entire property of the corporation and take payment in the shares of a new corporation and distribute them among the stockholders of the old corporation.[4] The implied power to wind up the business and make a sale of the property will probably authorize a sale for stock in another corporation.[5] As to an agreement whereby a corporation is to abandon its manufacturing business and restrict itself to the holding of the stock of another corporation by which it was to be carried on, the court said:[6] "The avowed object was to

[1] Holmes & Co. v. Holmes, etc., Co., 127 N. Y. 252.

[2] Talmage v. Pell, 7 N. Y. 328; First Nat'l Bank v. Exchange Nat'l Bank, 92 U. S. 122; McCutcheon v. Merz, etc., Co., 71 Fed. Rep. 787; Howe v. Carpet Co., 16 Gray 493; Hodges v. Screw Co., 1 R. I. 312, 53 Am. Dec. 624; Kennedy v. Bank, 101 Cal. 495; Knowles v. Sandercock, 107 Cal. 629.

[3] Memphis, etc., R. Co. v. Wood, 88 Ala. 630; National Bank v. Case, 99 U. S. 628; Holmes & Co. v. Holmes, etc., Co., 127 N. Y. 252. "A corporation having power to dispose of its property may also, as an incident to the exercise of this power, in some instances at least, determine what shall be accepted in payment, and may be justified in accepting the stock of another corporation for distribution among the stockholders of the first corporation according to their respective interests." Note to Denny, etc., Co. v. Schram, 36 Am. St. Rep. 140, citing Treadwell v. Salsbury, etc., Co., 7 Gray 393, 405, 66 Am. Dec. 490; Hodges v. New England, etc., Co., 1 R. I. 312, 347, 53 Am. Dec. 624. See Evans v. Bailey, 66 Cal. 112; Ryan v. Leavenworth, 21 Kan. 365.

[4] Treadwell v. Mfg. Co., 7 Gray (Mass.) 393.

[5] Holmes & Co. v. Holmes, etc., Co., 127 N. Y. 252; McCutcheon v. Merz, etc., Co., 71 Fed. Rep. 793.

[6] McCutcheon v. Merz, etc., Co., *supra;* Central Trans. Co. v. Pullman, etc., Co., 139 U. S. 24, 11 Sup. Ct. 478; Thomas v. Railway Co., 101 U. S. 71; People v. North River, etc., Co., 121 N. Y. 582, 24 N. E. Rep. 834; Mallory v. Oil Works, 86 Tenn. 598, 8 S. W Rep. 396.

continue corporate life and activity through the instrumentality of another corporation. There was to be a corporation within a corporation. Individual activity was to cease, but corporate energy was to be exercised through a living corporation, whose life and functions were to be controlled through the shares held by its corporate creator and master. Forbidden to exercise the very functions for which the breath of corporate life had been breathed into it, by the state, there would remain standing only the shell of the corporation, retaining corporate existence only for the purpose of controlling and directing the new corporation, in which was invested its corporate capital, and to receive and distribute its aliquot proportion of those dividends as earnings among its own shareholders. The effect of this action of the appellee was to divest itself of the power to exercise the essential and vital elements of its franchise, by a renunciation of the right to engage directly and individually in the very business which it was organized to carry on, and is a disregard of the conditions upon which its corporate existence was conferred. The state is presumed to grant corporate franchises in the public interest, and to intend that they shall be exercised through the proper officers and agencies of the corporation and does not contemplate that corporate powers will be delegated to others. Any conduct which destroys their functions, or maims or cripples their separate activity, by taking away the right to freely and independently exercise the functions of their franchise, is contrary to a sound public policy."

§ 192. **Purchase of its own shares.**—There is a conflict of authority as to whether a corporation has implied authority to purchase and hold its own stock. The law is settled in England that a corporation can not purchase shares of its own stock,[1] and the rule in the United States is that such a purchase is *ultra vires* at least when the effect is to reduce the capi-

[1] Trevor v. Whitworth, L. R. 12 App. Cas. 409; Zulueta's Claim, L. R. 5 Ch. App. Cas. 444; Hope v. International, etc., Soc., L. R. 4 Ch. Div. 327.

tal stock, and thus diminish the security of creditors.[1] The funds of an insolvent corporation certainly can not be used to purchase a portion of its capital stock, as it would be inequitable to the other stockholders and a fraud upon the creditors.[2] The fact that creditors did not know of the transaction when their debts were incurred is immaterial.[3] The general rule and its exceptions are thus stated by the supreme court of Ohio:[4] "The doctrine that corporations, when not prohibited by their charter, may buy and sell their own stock, is supported by a line of authorities; but nevertheless we think the decided weight of authority, both in England and in the United States, is against the existence of the power, unless conferred by express grant or clear implication. * * * It is true, however, that in most jurisdictions, where the right of a corporation to traffic in its own stock has been denied, an exception to the rule has been admitted to exist, whereby a corporation has been allowed to take its own stock in satisfaction of a debt due to it.[5] This exception is supposed to

[1] Augsburg, etc., Co. v. Pepper, 95 Va. 92, 27 S. E. Rep. 807. Such a purchase does not necessarily reduce the capital stock. It may be held by the corporation and reissued. State v. Smith, 48 Vt. 266; State Bank v. Fox, 3 Blatch. C. C. 431; Vail v. Hamilton, 85 N. Y. 453; American, etc., Co. v. Haven, 101 Mass. 398; Dupee v. Boston, etc., Co., 114 Mass. 37. In Lowe v. Pioneer, etc., Co., 70 Fed. Rep. 646, Nelson, J., said: "It is a mooted question in this country as to whether a corporation may purchase shares of its own stock; many states forbid it. In the absence of a charter prohibition, or a statute forbidding it, there is no reason why the stock should not be purchased, at least with the profits derived from the business of the corporation, where all the stockholders assent thereto. The tendency of the decisions in the state of Minnesota is on this line. See State v. Minn., etc., Co., 40 Minn. 227."

[2] Currier v. Lebanon, etc., Co., 56 N. H. 262; Alexander v. Rolfe, 74 Mo. 495; Adams, etc., Co. v. Dyette, 5 S. Dak. 418; Crandall v. Lincoln, 52 Conn. 73; In re Columbian Bank, 147 Pa. 422, 23 Atl. Rep. 626; Commercial, Nat'l Bank v. Burch, 141 Ill. 519, 31 N. E. Rep. 420. The receiver of an insolvent corporation may recover from a stockholder whose stock has been purchased by the corporation. Farnsworth v. Robbins, 36 Minn. 369; State v. Oberlin, etc., Assn., 35 Ohio St. 258; Price v. Coal Co. (Ky.), 32 S. W. Rep. 267.

[3] Commercial Nat'l Bank v. Burch, 141 Ill. 519.

[4] Coppin v. Greenless, 38 Ohio St. 275.

[5] Taylor v. Exporting Co., 6 Ohio 177; Coppin v. Greenless, 38 Ohio St. 273; Ex parte Holmes, 5 Cow. (N.Y.) 426; State v. Smith, 48 Vt. 266; Williams v. Mfg. Co., 3 Wd. Ch. 418; First Nat'l Bank v. Exchange Nat'l Bank,

rest upon a necessity which arises in order to avoid loss." So, in a case where a corporation in failing circumstances borrowed money with which to purchase its own shares, the court said:[1] "If a corporation, to the injury of creditors, can borrow money for the purchase of one share of its stock, or the stock held by one member, it can borrow money with which to purchase the shares of all its members, and thus destroy its very existence, as no corporation like the defendant can have an existence in this jurisdiction without stock and without stockholders. The doctrine is well established that a purchase of shares in itself by a corporation is against public policy and *ultra vires*, whenever such purchase diminishes its ability to pay its debts, or lessens the security of its creditors."[2]

§ 193. **When a corporation may hold its own shares.**—The weight of American authority seems to be in favor of the view that the act of purchasing its own shares of stock is not in it-

92 U. S. 122; City Bank v. Bruce, 17 N. Y. 507; Verplanck v. Mercantile, etc., Co., 1 Edw. Ch. (N.Y.) 84. May accept its own stock as a gift, Lake Superior, etc., Co. v. Drexel, 90 N. Y. 87.

[1] Adams, etc., Co. v. Dyette, 5 S. Dak. 418, 59 N. W. Rep. 214, 65 N. W. Rep. 471.

[2] German Sav. Bank v. Wulfekuhler, 19 Kan. 60; Gill v. Balis, 72 Mo. 424; Barton v. Plank, etc., Co., 17 Barb. 397; Clapp v. Peterson, 104 Ill. 26; State v. Oberlin, etc., Assn., 35 Ohio St. 258; Abeles v. Cochran, 22 Kan. 405; State of Minn. v. T. M. Co., 40 Minn. 213, 227; Johnson v. Bush, 3 Barb. Ch. 207; Morawetz I, § 112, *et seq.*; Spelling I, § 168; Beach II, § 395; Green's Brice Ultra Vires (2d Am. ed.), 94; Cook I, ch. 19. Mr. Taylor (§ 134) says: "In regard to the power of a corporation to purchase its own stock, there is a difference of opinion. The English decisions seem unanimously to negative the possession of this power by the corporation; and Mr. Brice's proposition — 'Corporations can not, whatever the nature of their business, without an express and very clear power in that behalf, deal in their own shares'—may be regarded as expressing somewhat vaguely, and from his use of the word 'deal,' the English law on the subject. In America, on the other hand, the weight of authority clearly indicates that there is nothing in itself illegal or *ultra vires* in the purchase of its own shares by a corporation; and that whether the purchase is valid depends on the condition of the corporate affairs, the purpose for which the purchase was made (or the shares received by the corporation) and on the relations to the corporation of the persons questioning the validity of the transactions."

self illegal, but that the validity of the particular transaction depends upon the condition of the corporate affairs, and the purpose for which the purchase was made.[1] It is held in some states that a corporation may purchase its own shares on condition that it is solvent and that the effect of the transaction is not to reduce its actual assets below its capital stock.[2] The purchase must not be made "at such time and in such manner as to take away the security upon which the creditors of the corporation have the right to rely for the payment of their claim, or, in other words, so as not to diminish the fund created for their benefit. Each case must therefore depend upon and be determined by its own facts and circumstances."[3] As said by Mr. Cook,[4] "If there is no statutory liability on the stock, and if stockholders do not object, there is no reason why the net profits of the corporation should not be applied to the purchase of stock instead of being used for dividends."

A corporation organized to deal in jewelry without any limitations as to what it may take in payment for its goods, may take payment in its own stock.[5] When shares are legally pur-

[1] Dupee v. Boston, etc., Co., 114 Mass. 37

[2] Leland v. Hayden, 102 Mass. 542, 551; American, etc., Co. v. Haven, 101 Mass. 398; Dupee v. Boston, etc., Co., 114 Mass. 37; Chicago, etc., Co. v. Marsailles, 84 Ill. 145, 643; Iowa, etc., Co. v. Foster, 49 Iowa 25. Subsequent creditors can not complain. Rollins v. Shaver Co., 80 Iowa 380; Taylor v. Miami, etc., Co., 6 Ohio 176; Bank v. Champlain, etc., Co., 18 Vt. 131; Pierce Railroads, 505. See Holliday v. Elliott, 8 Ore. 84; Preston v. Grand, etc., Co., 11 Sim. 327. In a late case, First Nat'l Bank v. Salem, etc., Co., 39 Fed. Rep. 89, Deady, J., said: "The rule appears to be well settled that a corporation may, unless prohibited by statute, purchase its own stock or take it in pledge or mortgage." Citing City Bank v. Bruce, 17 N. Y. 507; Taylor v. Exporting Co., 6 Ohio 177; In re Ins. Co., 3 Biss. 452; Bank v. Transportation Co., 18 Vt. 138; Dupee v. Boston, etc., Co., 114 Mass. 37. In Clapp v. Peterson, 104 Ill. 26, the rule was so laid down, with the qualification "that such act is had in entire good faith, is an exchange of equal value and is free from all fraud." The purchase of shares of its own stock by a corporation having power to do so does not operate as a reduction of its capital stock where the power to reduce its stock was not reserved. Western, etc., Co. v. Des Moines Nat'l Bank, 103 Iowa 455, 72 N.W. Rep. 657; Shoemaker v. Washburn, etc., Co., 97 Wis. 585, 73 N. W. Rep. 333.

[3] Fraser v. Ritchie, 8 Brad. (Ill.) 554; Vail v. Hamilton, 85 N. Y. 453; Iowa, etc., Co. v. Foster, 49 Iowa 25; Dock v. Cordage Co., 167 Pa. St. 370.

[4] Corps., § 311.

[5] White v. Marquardt (Iowa), 70 N. W. Rep. 193, 74 N. W. Rep. 930.

chased by the corporation, they may be reissued.[1] Unissued stock may, by agreement of all the stockholders, where there are no debts, be paid for with the money of the corporation, and issued to one of the stockholders as a trustee for all.[2]

§ 194. **Powers of national banks.**—The Revised Statutes of the United States[3] provide that "no association shall make any loan or discount on the security of the shares of its own capital stock, nor be the purchaser or holder of any such shares, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and stock so purchased or acquired shall, within six months from the time of its purchase, be sold or disposed of at public or private sale; or, in default thereof, a receiver may be appointed to close up the business of the association." While this section in terms prohibits a banking association from making a loan on security of shares of its own stock, it imposes no penalty either upon the bank or borrower if a loan upon such security is made. If the prohibition can be urged against the validity of the transaction by any one except the government, it can only be done before the contract is executed, while the security is still subsisting in the hands of the bank. It can then, if at all, be invoked to restrain or defeat the enforcement of the security. When the contract has been executed, the security sold and the proceeds applied to the payment of the debt, the court will not interfere with the matter. Both bank and borrower are in such case equally the subjects of legal censure, and they will be left by the court where they have placed themselves.[4]

§ 195. **Consolidation.**—The consolidation of corporations can take place only under proper legislative authority,[5] and

[1] State v. Smith, 48 Vt. 266; Common v. Boston, etc., R. Co., 18 Mass. 142.

[2] Jones v. Morrison, 31 Minn. 140.

[3] Rev. Stat. U. S., § 5201.

[4] Nat'l Bank, etc., v. Stewart, 107 U. S. 676.

[5] Clearwater v. Meredith, 1 Wall. (U. S.) 25; Pearce v. Madison, etc., R. Co., 21 How. (U. S.) 441; Cole v. Millerton, etc., Co., 133 N. Y. 164. A domestic corporation may be authorized to consolidate with a foreign corporation. Continental, etc., Co. v. Toledo, etc., R. Co., 82 Fed. Rep. 642. As to consolidation of Illinois and Indiana corporations, see an article in 12 Har. Law Rev. 486. Whether or not the legislature can authorize the

statutory requirements as to the proceedings are conditions precedent and must be complied with before there is a legal consolidation.[1] Thus, when a certificate of incorporation is required to be filed, it must, in order to be effectual, contain all the recitals required by the statute.[2] When all the other essential provisions of an act authorizing consolidation are complied with the consolidation is not invalidated by the mere absence of evidence that each company filed with the secretary of state a resolution accepting the provisions of the act, passed by a majority of the stockholders at a meeting called for that purpose, or that the stockholders held separate meetings for the purpose. The absence of such evidence is supplied by the implication arising from the certified copy of the articles of agreement for consolidation duly filed with the secretary of state.[3]

The authority to consolidate may be contained in the corporate charter,[4] a statute,[5] or it may be contained in the charter of the corporation with which the corporation in question is authorized to consolidate.[6] So, an unauthorized consolidation may be cured by acquiescence and legislative recognition.[7]

The majority of the stockholders of a corporation have no power to involve the minority in a reorganization without its consent, in such manner as to compel the minority to elect between a new contractual relation with a new company, or compensation for them on an arbitrary basis.[8]

consolidation of corporations under the general power reserved to alter or annul the charter, it certainly can not do so when the rights of stockholders will thereby be affected by increasing their liability as such or diminishing the value of their stock; unless the consolidation is made with the unanimous consent of all the stockholders. Botts v. Simpkinsville, etc., Co., 88 Ky. 54, 2 L. R. A. 594.

[1] Commonwealth v. Atlantic, etc., R. Co., 53 Pa. St. 9; Tuttle v. Michigan, etc., R. Co., 35 Mich. 247.

[2] State v. Vanderbilt, 37 Ohio St. 590.

[3] Leavenworth Co. v. Chicago, etc., R. Co., 25 Fed. Rep. 219.

[4] Nugent v. Supervisors, 19 Wall. (U. S.) 241.

[5] Black v. Delaware, etc., Co., 24 N. J. Eq. 455.

[6] In re Prospect Park, etc., Co., 67 N. Y. 371. But see Morrill v. Smith Co., 89 Tex. 529.

[7] Mead v. New York, etc., R. Co., 45 Conn. 199.

[8] Post v. Beacon, etc., Co. (C.C. App.), 84 Fed. Rep. 371. As to relations resulting from succession and reorganization instead of consolidation, see Kittel v. Augusta, etc., R. Co., 78 Fed.

§ 196. **The effect of consolidation.**—The result of consolidation is ordinarily, although not necessarily, the creation of a new corporation. The old corporations may or may not be dissolved, depending upon the legislative will,[1] or one corporation may be merely merged in another by the process of purchasing its shares and franchises under legislative authority. As a general rule, however, consolidation works a dissolution of the corporations previously existing and the creation of a new corporation with property, liabilities and stockholders different from those passing out of existence.[2] But a new corporation does not necessarily result, as there can be a union of interests and of stock without the surrender of personal identity or corporate existence.[3] This is always a question of legislative intent. The test, "in all cases is to be found from the facts and circumstances, terms of contracts, texts of statutes, intent of parties; from these it must be determined whether the original corporation passed out of existence, or remains under a new name and management with enlarged powers."[4]

§ 197. **Powers and privileges of the new corporation.**—The powers of the consolidated corporation are generally regulated by the statute authorizing consolidation.[5] Ordinarily, all the

Rep. 855; Ferguson v. Ann Arbor, etc., R. Co., 45 N. Y. Supp. 172; Santa Fe, etc., Co. v. Hitchcock (N. Mex.), 50 Pac. Rep. 332; Benesh v. Mill-Owners', etc., Co., 103 Iowa 465, 72 N. W. Rep. 674. To render a new corporation liable at common law for the debts of an established corporation or firm, to whose business and property it has succeeded, it must, in the absence of a special agreement, appear that the transaction was fraudulent as to creditors of the old corporation, or that the circumstances attending the creation of the new corporation and its succession to the business and property of the old corporation are of such a character as to warrant a finding that it is a mere continuation of the former. Austin v. Tecumseh Nat'l Bank, 49 Neb. 412, 68 N. W. Rep. 628, 35 L. R. A. 444.

[1] Keokuk, etc., R. Co. v. Missouri, 152 U. S. 301; Adams v. Yazoo, etc., R. Co. (Miss.), 24 So. Rep. 317.

[2] McMahon v. Morrison, 16 Ind. 173, 79 Am. Dec. 418; Pullman, etc., Co. v. Mo. Pac. R. Co., 115 U. S. 587; Railroad Co. v. Georgia, 98 U. S. 359; Shields v. Ohio, 95 U. S. 319; Kansas, etc., R. Co. v. Smith, 40 Kan. 192.

[3] Central R. Co. v. Georgia, 92 U. S. 665; Chicago, etc., R. Co. v. Ashling, 160 Ill. 373.

[4] Hirschl, Com. & Consol. of Corp., p. 184.

[5] See Shields v. Ohio, 95 U. S. 319

franchises of the old companies pass to the new, and this includes all the rights which before consolidation have accrued or vested in the old corporations.[1] Thus, a consolidated company is entitled to the benefit of a tax voted to one of the old companies by a county or township. At the time of the vote of the tax the railroad corporation had under the law authority to consolidate with the other corporations. After consolidation it was contended that the county was under no obligation to vote the tax for the benefit of the new corporation. The court said:[2] "The provisions for consolidation became part of the contract between the township and the railroad company, and the vote to issue the bonds to the company was an assent to the exercise by it of all the corporate powers, including that of consolidation, with which it was invested at the time of the vote." Hence, the new corporation is entitled to bonds voted to one of its constituents,[3] to the benefit of exemptions for its employes which were enjoyed by the former company,[4] to the constituent's exclusive right to supply gas,[5] to the power to hold lands,[6] to condemn lands under the power of eminent domain,[7] to the use of a street,[8] when these powers were possessed by one or all of the constituent companies. By

[1] Paine v. Lake Erie, etc., R. Co., 31 Ind. 283; Cooper v. Corbin, 105 Ill. 224; Louisville Trust Co. v. Louisville, etc., R. Co. (C. C. App.), 75 Fed. Rep. 433.

[2] Livingston Co. v. First Nat'l Bank, 128 U. S. 102. The court said: "We think that in the present case the rule applied in the cases before cited of County of Scotland v. Thomas, 94 U. S. 682; Town of East Lincoln v. Davenport, 94 U. S. 801; Wilson v. Salamanca, 99 U. S. 499; Menasha v. Hazard, 102 U. S 81; Harter v. Kernochan, 103 U. S. 562; New Buffalo v. Iron Co., 105 U. S. 73, and Bates County v. Winter, 112 U. S. 325, is the more proper and salutary one, and that the doctrine laid down in Harshman v. Bates County, 92 U. S. 569, and in the County of Bates v. Winter, 97 U. S. 83, that a county court in Missouri could not, on a vote by a township to issue bonds to a corporation named, issue bonds to a county formed by the consolidation of that corporation with another corporation, would not be, if applied here, a sound doctrine."

[3] Green Co. v. Conners, 109 U. S. 104; Niantic, etc., Bank v. Town of Douglass, 5 Ill. App. (Brad.) 579.

[4] Zimmer v. State, 30 Ark. 677.

[5] New Orleans Gas Co. v. Louisiana, etc., Co., 115 U. S. 650.

[6] Georgia, etc., R. Co. v. Wilks, 86 Ala. 478.

[7] Toledo, etc., R. Co. v. Dunlap, 47 Mich. 456; Abbott v. N. Y., etc., R. Co., 145 Mass. 450; State v. Sherman, 22 Ohio St. 411.

[8] Pittsburgh, etc., R. Co. v. Reich, 101 Ill. 157.

the weight of authority a consolidation which results in the creation of a new corporation, destroys an exemption from taxation which was possessed by one of the corporations.[1] A special statutory exemption or privilege does not pass in the absence of express statutory direction.[2] The consolidation effects an assignment of the choses in action of the old companies to the new,[3] and the title of the constituent companies to real property vests *ipso facto* in the new corporation.[4] The articles of consolidation may transfer the real estate of the old companies to a consolidated foreign corporation.[5]

§ 198. **Liabilities of the new corporation.**—The general rule is that the new corporation resulting from consolidation becomes liable for the debts, obligations, liabilities and torts of the old companies.[6] It has been held, however, that in the

[1] For an exhaustive discussion of this question, see Adams v. Yazoo, etc., R. Co. (Miss. 1898), 24 S. Rep. 371.

[2] As the right of a railroad company to determine its rate of fare. St. Louis, etc., R. Co. v. Gill, 156 U. S. 649.

[3] Univ. of Vt. v. Baxter, 42 Vt. 99, 43 Vt. 645.

[4] Cashman v. Brownlee, 128 Ind. 266.

[5] Tarpey v. Deseret Salt Co., 5 Utah 494.

[6] Paine v. Lake Erie, etc., R. Co., 31 Ind. 283; Indianapolis, etc., R. Co. v. Jones, 29 Ind. 465; State v. Baltimore, etc., R. Co., 77 Md. 489; Philadelphia v. Ridge Ave. R. Co., 143 Pa. St. 444; Lake Shore R. Co. v. Hutchins, 37 Ohio St. 282; Chicago, etc., R. Co. v. Moffatt, 75 Ill. 524. In Louisville, etc., R. Co. v. Boney, 117 Ind. 501, 3 L. R. A. 435, the court says: "While it is an open question in some jurisdictions whether or not, in the absence of a statute, the debts of the original companies follow as an incident of consolidation and become by implication the obligations of the new corporation, it is settled in this state that the act of consolidation involves an implied assumption by the new company of all the valid debts and liabilities of the consolidated companies. Indianapolis, etc., R. Co. v. Jones, 29 Ind. 465; Columbus, etc., R. Co. v. Powell, 40 Ind. 37; Jeffersonville, etc., R. Co. v. Hendricks, 41 Ind. 48; Cleveland, etc., R. Co. v. Prewitt, 134 Ind. 557, 33 N. E. Rep. 367. The rule which the authorities support seems to be that where one corporation goes entirely out of existence by being incorporated into another, if no arrangements are made respecting the property and liabilities of the corporation that ceases to exist, the corporation into which it is merged will succeed to all its property, and be answerable for all its liabilities. Thompson v. Abbott, 61 Mo. 176; Mt. Pleasant v. Beckwith, 100 U. S. 514; Pullman, etc., Co. v. Mo. Pac. R. Co., 115 U. S. 587. A consolidated railway company may be held responsible for the acts and neglects of its constituent members to the same extent as though done by it as a whole. Southern R. Co. v. Bourknight, 70 Fed. Rep. 442, 30 L.

absence of a statutory imposition, the new corporation is liable to the creditors of the old only in respect to the property received from it.[1] Under this theory, as to the property received from the other corporations, it is a new and independent corporation, liable for the claims of creditors only by virtue of the assumption of the obligation, or a statutory imposition. The new company may, of course, be required to assume all the obligations of the old company, and this imposition may be imposed by the statute or by contract.[2] The sound rule is that a successor corporation, which succeeds to the property, must take the obligations with the benefits.[3] This rule is particularly applicable in jurisdictions where it is held that a creditor can not prevent a corporation which owes him money from consolidating. Where the statute authorizes consolidation and makes no provision to the contrary, the creditor may follow the property into the hands of the consolidated company.[4] Under an express contract of assumption of the debts of the old companies, a corporation is liable for damages to land caused by one of the old companies,[5] for labor performed for one of the old companies,[6] and is bound by an agreement allowing other railroads to use its right of way. Where the statute preserves all the rights of the creditors of the original company, bondholders of the new company are bound by an unrecorded contract of one of the original companies under which it bound

R. A. 823. The right of a creditor to recover his claim against a consolidated company under N. Y. Laws, 1892, ch. 691, is not defeated by the recovery of a judgment upon the claim against the constituent corporation. In re Utica, etc., Co., 154 N. Y. 268.

[1] Prouty v. Lake Shore, etc., R. Co., 52 N. Y. 363. A corporation which purchases all the property of another corporation, and gives its stock in payment therefor to the stockholders of the vendor corporation, takes the property subject to the rights of the creditors Grenell v. Detroit, etc, Co., 112 Mich. 70, 70 N. W. Rep. 413.

[2] Warren v. Mobile, etc., R. Co., 49 Ala. 582; Western, etc., R. Co. v. Smith, 75 Ill. 496; New Bedford, etc., R. Co. v. Old Colony R. Co., 120 Mass. 397; John Hancock, etc., Co. v. Railway Co., 149 Mass. 214; Day v. Worcester, etc., R. Co., 151 Mass. 302; Polhemus v. Fitchburg R. Co., 123 N. Y. 502.

[3] Montgomery, etc., R. Co. v. Baring, 51 Ga. 582.

[4] Shackelford v. Mississippi, etc., R. Co., 52 Miss. 159.

[5] Smith v. Los Angeles Co., 98 Cal. 210.

[6] Western, etc., Co. v. Smith, 75 Ill. 497.

itself to have a flag station and to allow the use of land to the grantor of a right of way.[1] But a consolidated company can not be rendered liable for the debts of the old company by an act passed after the consolidation when property of the original company creating the debt had been sold under a deed of trust prior to the consolidation.[2]

The purchaser of a railroad at a decretal sale takes the property free from a condition imposed by a county in granting aid to the effect that trains should stop at a certain station. The new company, however, is subject to the common law requirement that it must stop sufficient trains at the station for the purpose of transacting the business.[3]

A railroad company formed by consolidation of others, one of which was organized by the purchasers of a railroad at foreclosure, is bound by the obligation of the original company to pay for land that it appropriated under a parol license and agreement to pay for it. The court said[4] that the "action was brought on the theory, not of a breach of agreement made by the old company and the plaintiff, but for a breach of equitable duty laid on the defendant by force of the facts that it had taken the plaintiff's land, and is taking and using it in the same plight that its predecessor held it, and that the plaintiff is entitled to and is without compensation. The new company is enjoying the easement under the conditions of the old company and the benefits and burdens incident to it are inseparable." The specific performance of a contract made by a constitutent company may be enforced against the new consolidated company.[5]

§ 199. **Loaning of money.**—A corporation can not engage in the loaning of money unless authorized to do so by its charter, or unless its business is of a nature which usually involves the making of loans.[6] But money so illegally loaned

[1] Mobile, etc., R. Co. v. Gilmer, 85 Ala. 422.

[2] Hatcher v. Toledo, etc., R. Co., 62 Ill. 477.

[3] People v. Louisville, etc., R. Co., 120 Ill. 48.

[4] Chicago, etc., R. Co. v. Hall, 135 Ind. 91, 23 L. R. A. 231.

[5] Cumberland Valley R. Co. v. Gettysburg, etc., R. Co., 177 Pa. St. 519.

[6] Daniel Neg. Inst. I, § 384; Cook II, § 690.

can be recovered, and the borrower can not interpose the defense of the want of power in the corporation to make the loan.[1] The franchise of the corporation may be forfeited at the instance of the state, but the money loaned may be recovered.[2]

§ 199*a*. **Power to act as trustee.**—Whether a corporation may undertake the performance of a trust depends upon the provisions of its charter and the circumstances of the particular case. "Although it was in early times held that a corporation could not take and hold real and personal estate in trust, upon the ground that there was a defect of one of the requisites of a good trustee, namely, the want of confidence in the person; yet that doctrine has long since been exploded as unsound and too artificial; and it is now held that where a corporation has a legal capacity to take real and personal estate, there it may take and hold it upon trust in the same manner and to the same extent as a private individual may do."[3]

[1] Poock v. Lafayette, etc., Assn., 71 Ind. 357; Bond v. Terrell, etc., Co., 82 Tex. 309; 18 S. W. Rep. 691; Steam, etc., Co. v. Weed, 17 Barb. 382; Union, etc., Co. v. Murphy's, etc., Co., 22 Cal. 621; Gold, etc., Co. v. National Bank, 96 U. S. 640; Smith v. White (Tex.), 25 S. W. Rep. 809; Kadish v. Garden City, etc., Assn., 47 Ill. App. 602. *Contra:* Grand Lodge v. Waddell, 36 Ala. 313; Chambers v. Falkner, 65 Ala. 448; Life Ins. Co. v. Mech., etc., Co., 7 Wend. 31; New York, etc., Co. v. Ely, 5 Conn. 560.

[2] Shoemaker v. Mech. Nat'l Bank, 2 Abb. (U. S.) 416; Elder v. Bank, etc., 12 Kan. 238.

[3] Judge Story, in Vidal v. Girard, 2 How. (U. S.) 187; White v. Rice, 112 Mich. 403, 70 N. W. Rep. 1024. "The ability and competency to execute the trust is the real test in determining whether a corporation may take." Spelling I, § 212. See Chapin v. School Dist., 35 N. H. 445; Philip Academy v. King, 12 Mass. 546; In re Howe, 1 Paige 214. Without express authority a corporation can not act as executor or administrator. Georgetown, etc., v. Brown, 34 Md. 450. A corporation can not be a partner. People v. N. R. S. R. Co., 121 N. Y. 582.

CHAPTER 9.

THE DOCTRINE OF ULTRA VIRES AND ITS APPLICATION.

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§ 200. **General statement.**—The phrase *ultra vires* has been in general use to describe the acts of corporations and their officers which are in excess of the corporate power.[1] Much con-

[1] Power here signifies authority, legal competence, capacity or right. In Bissell v. Mich., etc., R. Co., 22 N. Y. 258, Comstock, J., said: "To say that a corporation has no right to do unauthorized acts is to put forth a very plain truism; but to say that such bodies have no power or capacity to err, is to impute to them an excellence which does not belong to any created

fusion has resulted from its use to express acts in excess of the authority conferred upon the corporation, and acts which are illegal in the sense of being prohibited by law. An act which is in excess of the authority of an agent or officer of a corporation is not, upon well established principles of the law of agency, binding upon the corporation. There is nothing peculiar to the law of corporations in this; and the use of the phrase *ultra vires* in this connection is confusing and misleading. There is also a division of authorities upon the question of the use of the phrase to describe acts which are illegal in the sense of being *malum per se* and *malum prohibitum*. It seems that it would be better to use the words to describe only such contracts of corporations as are in excess of their corporate powers. In considering the defense of *ultra vires*, however, it must be noted that a distinction is made between contracts which are (1) unauthorized because not granted expressly or by implication, (2) contracts which are merely an irregular exercise of a granted power, (3) contracts which are intrinsically immoral or against public policy, *malum in se*, and (4) contracts which are prohibited by the charter or general law, *malum prohibitum*.

§ 201. **Proper use of the phrase ultra vires.**—With reference to the proper use of this phrase, it was said by Justice Allen:[1] "When acts of corporations are spoken of as *ultra vires*, it is not intended that they are unlawful, or even such as the corporation can not perform, but merely those which are not within the powers conferred upon a corporation by the act of its creation."

existences with which we are acquainted. The distinction between power and right is no more to be lost sight of in respect to artificial than in respect to natural persons." A corporation, like a natural person, can do wrong, although not authorized to do so. See Salt Lake City v. Hollister, 118 U. S. 256, 2 C. C. 107; Life, etc., Co. v. Mechanic, etc., Co., 7 Wend. (N. Y.) 31. As said in Wright v. Hughes, 119 Ind. 324: "Corporations, like natural persons, have power and capacity to do wrong. They may, in their contracts and dealings, break over the restraints imposed by their charters; and when they do their exemption from liability can not be claimed on the mere ground that they have no attributes or faculties which render it possible for them thus to act."

[1] Whitney, etc., Co. v. Barlow, 63 N. Y. 62.

In a recent case in New Jersey,[1] Justice Depue said: "The indiscriminate use of this expression with respect to cases different in their nature and principles, has led to considerable confusion if not misapprehension. Where an act done by directors or officers is simply beyond the powers of the executive department of the corporation, the agency by which the corporation exercises its functions, and not of the corporation itself, it may be made valid and binding by the action of the board of directors or by the approval of the stockholders. Where the act done by the directors is not in excess of the powers of the corporation itself, but is simply an infringement upon the rights of other stockholders, it may be made binding upon the latter by ratification, or by consent implied by acquiescence. Where the infirmity of the act does not consist in a want of corporate power to do it, but in the disregard of formalities prescribed, it may or may not be valid as to third persons dealing bona fide with the corporation, according to the nature of the formalities not observed or the consequences the legislature has imposed upon non-observance. These are all cases depending upon legal principles not peculiarly applicable to corporations, and the use of the phrase *ultra vires* tends to confusion and misapprehension. In its legitimate use, the expression *ultra vires* should be applied only to such acts as are beyond the powers of the corporation itself." The proper scope of the doctrine is thus stated by Mr. Justice Brewer:[2] "Two propositions are settled. One is that a contract by which a corporation disables itself from performing the functions and duties undertaken and imposed by its charter is, unless the state which created it consents, *ultra vires*. A charter not only grants rights, it also imposes duties. An acceptance of those rights is an assumption of those duties. As it is

[1] Camden, etc., R. Co. v. May's Landing, etc., Co., 48 N. J. L. 530, in a dissenting opinion. But in many cases contracts which are merely beyond the power of the corporation are called illegal. See Central, etc., Co. v. Pullman, etc., Co., 139 U. S. 24; People v. Chicago, etc., Co., 130 Ill. 285; State v. Nebraska, etc., Co., 29 Neb. 700; Franklyn v. Lewiston Inst., 68 Maine 43.

[2] Chicago, etc., R. Co. v. Union Pac. R. Co., 47 Fed. Rep. 15. See statement by Mr. Justice Mitchell, in Minnesota, etc., Co. v. Langdon, 44 Minn. 43.

a contract which binds the state not to interfere with those rights, so, likewise it is one which binds the corporation not to abandon the discharge of those duties. It is not like a deed or patent which vests in the grantee or patentee not only title, but the full power of alienation. But it is more—it is a contract whose obligations neither party, state nor corporation can, without the consent of the other, abandon. The other is that the powers of corporation are such, and such only, as the charter confers, and an act beyond the measure of those powers, as either expressly stated or fairly implied, is *ultra vires*. A corporation has no natural or inherent rights or capacities. Created by the state, it has such powers as the state has seen fit to give it, 'only this and nothing more.' And so, when it assumes to do that which it has not been empowered by the state to do, its assumption of power is vain; the act is a nullity, the contract is *ultra vires*. These two propositions embrace the whole doctrine of *ultra vires*. They are its *alpha* and *omega*. Were the two foregoing propositions steadily kept in view by the courts in applying this doctrine, the diversity of judicial opinion on this subject would be much less.''

§ 202. **The strict rule.**—It follows from the doctrine of limited capacities that a corporation has only such powers as are expressly or by necessary implication granted to it. The theory is that the state is granting a favor, and the grantee takes only what is granted. As the corporation is able to exercise its powers by virtue of the grant alone, it follows that all attempts to exercise powers not granted are ineffectual as against the grantor. If the granted privileges are abused the state may withdraw them. And it would be extremely illogical for the state through its courts to aid those who enter into unauthorized relations with its creatures to carry out such unauthorized acts. As against the corporation in such cases the duty of the state is clear. But when innocent third persons become involved there is often a conflict between logical consistency and justice to the individual, and as a result the American law seems to be in a state of hopelessly in-

extricable confusion. The English decisions apply the doctrine that *ultra vires* acts are illegal with much more strictness than the American decisions. But practically the same rule is enforced by the federal courts. According to this rule, "A contract of a corporation which is either unauthorized by or in violation of its charter or governing statutes, or which is entirely outside the scope of the powers of its creation, is void in the sense of being no contract at all,[1] because of the want of power in the corporation to enter into it; that such a contract will not be enforced by any species of action in a court of justice,[2] that being void *ab initio*, it can not be made good by ratification,[3] or by any succession of renewals, and that no performance on either side can give validity to it so as to give a party to the contract any right of action upon it."[4] Under this rule, "The contracts of corporations which are not authorized by their charter are illegal, because they are made in contravention of public policy." Although the "unauthorized contract may be neither *malum in se* nor *malum prohibitum*, but on the contrary may be for some benevolent or worthy object, * * * yet if it is a violation of public policy for corporations to exercise powers which have not been granted to them, such contracts, notwithstanding their praiseworthy nature, are illegal and void."[5] No action can be maintained on such a contract, although there has been part performance or expenses in-

[1] Davis v. Old Colony R. Co., 131 Mass. 258; Chicago, etc., Co. v. The People's, etc., Co., 121 Ill. 530; Franco, etc., Co. v. McCormick, 85 Tex. 416; Long v. Georgia, etc., R. Co., 91 Ala. 519; Twiss v. Guaranty, etc., Assn. (Iowa), 55 N. W. Rep. 8.

[2] Greenville, etc., Co. v. Planters', etc., Co., 70 Miss. 669; Pearce v. The Madison, etc., R. Co., 21 How. (U. S.) 441; Brunswick, etc., Co. v. United Gas, etc., Co., 85 Me. 532; Elevator Co. v. Memphis, etc., R. Co., 85 Tenn. 703.

[3] California Bank v. Kennedy, 167 U. S. 362. Nor by the assent of all the stockholders. In East Anglian R. Co. v. Eastern, etc., R. Co., 11 C. B. 775, 7 Eng. Law and Eq. Rep. 505. Jervis, C. J., said of a contract not within the authority of the corporation, "the assent of all the shareholders to such a contract, though it may make them all personally liable to perform such contract, would not bind them in their corporate capacity, or render liable their corporate funds." Germania, etc., Co. v. Boynton, 71 Fed. Rep. 797, 19 C. C. A. 118.

[4] Thompson Priv. Corp., § 5355, 13 Am. L. Rev. 632, 5 Am. L. Rev. 272, 282, 12 Cent. L. J. 386.

[5] See Bissell v. Michigan, etc., R. Co., 22 N. Y. 258.

curred on the faith of the *ultra vires* promise.[1] An action, however, in disaffirmance, may be maintained. An exception is sometimes made in favor of those who deal with a corporation without notice, actual or constructive, of the *ultra vires* character of the contract.[2] And a distinction is made between contracts for which there is no authority and contracts within the general scope of the authority, but in excess thereof in some particular.

§ 203. **The reasons for the rule.**—The reasons upon which the doctrine of *ultra vires* rests are thus stated by Mr. Justice Gray:[3] "The reason why a corporation is not liable upon a contract *ultra vires*, that is to say, beyond the powers conferred upon it by the legislature, and varying from the objects of its creation, as declared in the law of its organization, are:

"(1) The interest of the public that the corporation shall not transcend the powers granted.

"(2) The interest of the stockholders that the capital shall not be subjected to the risk of enterprises not contemplated by the charter, and therefore not authorized by the stockholders in subscribing for stock.

"(3) The obligation of every one entering into a contract with a corporation to take notice of the legal limits of its powers."

In an Iowa case, the court said:[4] "Corporations and offi-

[1] Davis v. Old Colony, etc., R. Co., 131 Mass. 258; Downing v. Mt. Washington Road Co., 40 N. H. 230; Central, etc., Co. v. Pullman, etc., Co., 139 U. S. 24.

[2] Miners', etc., Co. v. Zellerbach, 37 Cal. 543; Lucas v. Transfer Co., 70 Iowa 541; Humphrey v. Association, 50 Iowa 607; Boyce v. Coal Co., 37 W. Va. 73.

[3] Pittsburg, etc., R. Co. v. Keokuk, etc., Co., 131 U. S. Rep. 371. See statement of Cooley, J., in Day v. Spiral, etc., Co., 57 Mich. 146, 58 Am. Rep. 352.

[4] Lucas v. White Line, etc., Co., 70 Iowa 541, 59 Am. Rep. 449, 453. In McCormick v. Market Nat. Bank, 165 U. S. 538, the court said: "The doctrine of *ultra vires*, by which a contract made by a corporation beyond the scope of its corporate powers is unlawful and void and will not support an action, rests, as this court has often recognized and affirmed, upon three distinct grounds: The obligation of any one contracting with a corporation to take notice of the legal limits of its powers; the interest of the stockholders not to be subjected to risks which they have never under-

cers do not always keep within their powers, and the application of the doctrine of *ultra vires* is often attended with very perplexing questions. By the application of a few plain rules, however, we may readily reach the proper answer to the questions involved in the case. (1) Every person dealing with a corporation is charged with knowledge of its powers as set out in its recorded articles of incorporation. (2) Where a corporation exercises power not given by its charter it violates the law of its organization, and may be proceeded against by the state through its attorney-general, as provided by the statute, and the unanimous consent of all the stockholders can not make illegal acts valid. The state has the right to interfere in such cases. (3) Where a third party makes with the officers of a corporation an illegal contract beyond the powers of a corporation, *as shown by its charter*, such third party can not recover; because he acts with knowledge that the officers have exceeded their powers, and between him and the corporation or its stockholders no amount of ratification by those unauthorized to make the contract will make it valid. (4) Where the officers of a corporation make a contract with third parties in regard to matters apparently within their corporate powers, but which, upon the proof of extrinsic facts of which the parties had no notice, lie beyond their powers, the corporation must be held, unless it may avoid liability by taking timely steps to prevent loss or damage to such third parties; for in such cases the third party is innocent, and the corporation or stockholders less innocent for having selected officers not worthy of the trust reposed in them."

§ 204. **Conflicting theories and decisions—More liberal doctrine.**—There has always been a strong current of opposition to the application of the rule as stated by Mr. Justice Gray and applied in cases which follow the lead of the supreme court of the United States. The doctrine originated at a time when corporations were created for public purposes only, and its

taken; and, above all, the interest of the public that the corporation shall not transcend the powers conferred upon it."

early development was with reference to the transactions of municipal corporations. It is properly applied with great strictness to the transactions of public corporations,[1] but many of the reasons urged for its application to the contracts of purely private corporations are somewhat fanciful in these times of free incorporation. Scarcely any two text writers agree upon a consistent theory of *ultra vires*. Judge Thompson has nothing but hard words for the strict doctrine and the courts which enforce it;[2] while Mr. Reese is equally certain that only through its rigid enforcement can our legal salvation be worked out.[3] The strict doctrine is most consistently adhered to by the federal courts, but in the most of the state courts the rule that *ultra vires* contracts of corporations are illegal and void is repudiated. Under these decisions want of authority alone does not render a contract illegal and hence void.[4] If it is founded upon a good consideration and is not void because prohibited by law, it is voidable only, and may give rise to rights of action, although the corporation did not have authority to make it. The courts accepting this doctrine hold that "the plea of *ultra vires* should not as a general rule prevail, whether it is interposed for or against the corporation, when it would not advance justice, but on the contrary would accomplish a legal wrong."[5] Hence, if the condition of the parties is such that it would be inequitable to allow the defense of *ultra vires*, the doctrine of estoppel will be applied in such manner as to preclude the defense.[6] It would seem that the

[1] Young v. Board of Education, 54 Minn. 385, 40 Am. St. Rep. 340; Newbery v. Fox, 37 Minn. 141, 51 Am. St. Rep. 830; Elliott Pub. Corp., § 288, and cases cited.

[2] Thompson Priv. Corp., § 5969.

[3] Reese *Ultra Vires*, ch. III. See 11 Harv. Law Rev. 387, article on Non-public Corporations and *Ultra Vires*.

[4] See a discussion of the authorities in an article in 12 Cent. L. J. 386, by J. C. Harper.

[5] Whitney, etc., Co. v. Barlow, 63 N. Y. 62; Kadish v. Association, 151 Ill. 531.

[6] Bissell v. Railroad Co., 22 N. Y. 258; Parish v. Wheeler, 22 N. Y. 494; Holmes, etc., Co. v. Holmes, etc., Co., 127 N. Y. 252; Bradley v. Ballard, 55 Ill. 413; Heims, etc., Co., v. Flannery, 137 Ill. 309; Day v. Spiral Springs, etc., Co., 57 Mich. 146, 58 Am. Rep. 352; Dewey v. Railway Co., 91 Mich. 351; Wright v. Hughes, 119 Ind. 324; Seymour v. Society, 54 Minn. 147; Magee v. Improvement Co., 98 Cal.

following statement of the doctrine by Mr. Taylor could not be improved.[1] "An act beyond the scope of its corporate powers, if done on behalf of a corporation, or if done by the body corporate itself, affects the rights of persons in respect of the corporate enterprise only in so far as the possessors of those rights by their own acts or omissions have estopped themselves from asserting their rights; provided the acts be of such a character that the party dealing with the corporation or its agent could from an examination of the charter or enabling statute and articles of association have ascertained that the act was *ultra vires*."

§205. **Actions in furtherance of ultra vires contracts.**— When an *ultra vires* contract has been fully executed on both sides, neither party thereto can be heard to assert its invalidity as ground for relief against it.[2] According to the weight of authority, where the contract has been fully executed by one party the defense of *ultra vires* is not available in an action by the other to recover the agreed consideration, so long as the benefits which have been received are retained. When the contract, the performance of which is demanded by the plaintiff, consists in itself of something beyond the powers of the corporation, or otherwise unlawful, so that, in order for the action to proceed, something further unlawful must be done, then it seems that the action can not be maintained.[3] Thus, a suit for specific performance of an *ultra vires* contract to convey real estate can not be maintained.[4] The rule is apparently without exception that an action can not be maintained on an *ultra vires* contract under circumstances where the doctrine of estoppel can not be invoked. But according to one line of authorities, the parties may "be estopped in some cases from disputing the validity of a corporate contract

678; Union, etc., Co. v. Plume, etc., Co., 58 Conn. 219; Manchester, etc., R. Co. v. Concord, etc., R. Co., 66 N. H. 100.

[1] Taylor Priv. Corp., § 265.

[2] Long v. Georgia, etc., R. Co., 91 Ala. 519, 24 Am. St. Rep. 931; Holmes, etc., Co. v. Holmes, etc., Co., 127 N. Y. 252; Day v. Spiral Springs, etc., Co., 57 Mich. 146, 58 Am. Rep. 352.

[3] Thompson Priv. Corp., § 6024.

[4] Bank of Mich. v. Niles, 1 Doug. (Mich.) 401.

when it has been fully performed on one side, and when nothing short of its performance will do justice.'"[1]

§ 206. **Buckeye Marble Co. v. Harvey.**—This case contains an elaborate discussion of the doctrine of *ultra vires*. It was an action brought to enforce a claim which grew out of a contract by which one corporation agreed to purchase the shares of another corporation which was engaged in a similar business. It was held that the contract was *ultra vires* and void; and that no rights resulted from it which were enforcible in the courts.[2] The court said:

"The complainant sues upon the contract, and in affirmance of it, seeks to have this defendant perform an agreement which sprang from and was collateral to it. It has received the shares it purchased, and holds on to them. It simply asks that the defendant be further compelled to perform his contract by contributing in accordance with his agreement, his proportion of the liability paid off by complainant in protection of the property of the McMillan Marble Company. The suit is clearly in furtherance of the original, unlawful and void contract. That the contract has been executed by the plaintiff does not make it lawful or entitle it to an enforcement of it.

"This proposition was very plainly put in Pittsburgh, etc., R. Co. v. Keokuk, etc., Co.,[3] when it was stated as a result of all the previous decisions of that court upon this subject, 'that a contract made by a corporation, which is unlawful and void because beyond the scope of its corporate power, does not, by being carried into effect, become lawful and valid; but the proper remedy of the party aggrieved is by disaffirming the contract and sue to recover, on a *quantum meruit*, the value of what the defendant has actually received.'"

§ 207. **Central Transportation Co. v. Pullman Palace Car Co.**—This well-known case[4] involved a consideration of the cir-

[1] Cooley, C. J., in Day v. Spiral Springs, etc., Co., 57 Mich. 146, 58 Am. Rep. 352.

[2] 92 Tenn. 115, 18 L. R. A. 252.

[3] 131 U. S. 371.

[4] 139 U. S. 24. See a review of this case in Yale Law Journal, 1898. See also the sequel to this case in Pullman, etc., Co. v. Central, etc., Co., 171 U. S. 138. In Marble Co. v. Harvey, 92

cumstances under which a defendant may interpose the defense of *ultra vires* notwithstanding the fact that the contract has been fully performed by the other party. The transportation company had leased and transferred all of its property of every kind to the defendant company, which was engaged in a similar and competitive business. The lessee company undertook to pay all of the debts of the lessor company, and to pay to it annually the sum of $264,000 for a term of ninety-nine years. Possession was taken and the installments paid for a number of years. The suit was for a part of the installment for the last year before suit. The defense of *ultra vires* was interposed and sustained, the court holding that the sale was unauthorized and in excess of the power of the selling company. It was urged for the plaintiff, that even if the contract was void, because *ultra vires* and against public policy, yet that, having been fully executed on the part of the plaintiff, and the benefits of it received by the defendant for the period covered by the declaration, the defendant was estopped to set up the invalidity of the contract as a defense to an action to recover the compensation agreed on for that period.

After reviewing the decisions upon this branch of the case, the court said:

"The view which this court has taken of the question presented by this branch of the case, and the only view which ap-

Tenn. 115, the court said: "The passage cited by counsel from Railway Co. v. McCarthy, 96 U. S. 267, 'that the doctrine of *ultra vires* when invoked for or against a corporation should not be allowed to prevail when it would defeat the ends of justice or work a legal wrong,' is misleading and if literally construed would result in an enormous practical extension of the power of corporations. We do not understand that a result required by adherence to the law would be either unjust or a legal wrong. The learned judge doubtless intended it to be understood that the defense would be a legal wrong only when the law did not require its consideration by the court. This passage and one of similar character in San Antonio v. Mahaffy, 96 U. S. 312, was uncalled for in the case in which it was used and in Central, etc., Co. v. Pullman, etc., Co. was characterized as a mere passing remark. To sustain suit as now presented would be in affirmance and furtherance of an unlawful and void contract. It is in no sense a suit in disaffirmance."

pears to us consistent with legal principles, is as follows: A contract of a corporation which is *ultra vires* in the proper sense, that is to say, outside the object of its creation as defined in the law of its organization, and therefore beyond the powers conferred upon it by the legislature is not voidable only, but wholly void, and of no legal effect. The objection to the contract is not merely that the corporation ought not to have made it, but that it could not make it. The contract can not be ratified by either party because it could not have been authorized by either. No performance on either side can give the unlawful contract any validity, or be the foundation of any right of action upon it. When a corporation is acting within the general scope of the powers conferred upon it by the legislature, the corporation, as well as persons contracting with it, may be estopped to deny that it has complied with the legal formalities which are prerequisite to its existence or to its action, because such requisites might in fact have been complied with. But where the contract is beyond the powers conferred upon it by existing law, neither the corporation nor the other party to the contract can be estopped by assenting to it or by acting upon it, to show that it was prohibited by law.

"A contract *ultra vires* being unlawful and void, not because it is in itself immoral, but because the corporation, by the law of its creation, is incapable of making it, the courts, while refusing to maintain any action upon the unlawful contract, have always striven to do justice between the parties, so far as it could be done consistently with adherence to law, by permitting property or money parted with on the faith of the unlawful contract to be recovered back or compensation to be made for it. In such cases, however, the action is not maintained upon the unlawful contract, nor according to its terms, but on an implied contract of the defendant to return, or failing to do that, to make compensation for property or money which it has no right to retain. To maintain such an action is not to affirm, but to disaffirm, the unlawful contract."

§ 208. **Disaffirmance after part performance.**—The right and duty of a party to disaffirm an *ultra vires* contract after it

has been partially performed without being responsible in damages for the value of the unexecuted portion of the contract, is thus stated by Mr. Justice Miller:[1] "What is sought in the case before us is the enforcement of the unexecuted part of the agreement. So far as it has been executed * * * the accounts have been adjusted and each party has received what he was entitled to by its terms. There remains unperformed the covenant to arbitrate with regard to the value of the contract. It is the damages provided for in that clause of the contract which are sued for in this action—damages for a material part of the contract never performed; damages for the value of a contract which was void. It is not a case of a contract fully executed. * * * It is a contract forbidden by public policy and beyond the power of the defendant to make. Having entered into the agreement it was the duty of the company to rescind or abandon it at the earliest moment. This duty was independent of the clause in the contract which gave them the right to do it. Though they delayed its performance for several years, it was, nevertheless, a rightful act when it was done. Can this performance of a legal duty, a duty both to stockholders of the company and to the public, give to plaintiffs a right of action? Can they found such a right on an agreement void for want of corporate authority and forbidden by the policy of the law? To hold that they can, is, in our opinion, to hold that any act performed in executing a void contract makes all its parts valid, and that the more that is done under a contract forbidden by law, the stronger is the claim to its enforcement by the courts."

§ 209. **Recovery of consideration paid.**—As already stated, the courts will not interfere with an executed *ultra vires* contract.[2] But the injustice which results from permitting a corporation to plead *ultra vires*, while retaining benefits received under a partly executed contract, has led the courts which enforce the strict rule that an *ultra vires* contract is illegal and void to hold that, while no action can be maintained upon the

[1] Thomas v. Railroad Co., 101 U. S. 71.

[2] Long v. Railway Co., 91 Ala. 519, and cases cited in next note.

contract, the other party may disaffirm the contract and recover the value of what has been actually delivered. This may be done in an action *quasi ex contractu* or in a proper case, in a suit for an accounting of benefits received.[1] Thus, a manufacturing company purchased materials for the purpose of selling them again on speculation, and the vendor after delivering a part repudiated the contract and sued to recover the value of what had been delivered. Mr. Justice Cooley said:[2] "It will be observed that the contract though void in law involved no element of criminality and nothing

[1] Pittsburgh, etc., R. Co. v. Keokuk, etc., Co., 131 U. S. 371; Miller v. Insurance Co., 92 Tenn. 167, 21 S. W. Rep. 39; Brunswick, etc., Co. v. United, etc., Co., 85 Me. 532; Pennsylvania R. Co. v. St. Louis, etc., R. Co., 118 U. S. 290; Central, etc., Co. v. Pullman, etc., Co., 139 U. S. 24; California Bank v. Kennedy, 167 U. S. 362. In Greenville, etc., Co. v. Planters', etc., Co., 70 Miss. 669, it was held that an *ultra vires* contract would not be specifically enforced in equity, nor would an action at law lie thereon. The court, by Cooper, J., said: "The agreement between the directors of their companies was clearly beyond the corporate powers of either company to make, and it had not been fully executed when the appellant withdrew from it. There are some decisions which proceed on the apparent postulate that an *ultra vires* agreement executed fully by one of the corporations, or so far executed that the *status quo* can not be restored, may be made the basis of an action. But in many of these cases it would be found that the measure of recovery would be the same whether the injury to the plaintiff by the failure of the defendant to perform, or the benefit received by the defendant under the agreement is taken as the standard. Cases of this sort may therefore be well assigned to that other and far more numerous class in which the right of recovery is not rested upon the invalid agreement, but is recognized to exist notwithstanding the agreement upon the principle that the defendant may not repudiate the contract and yet retain the benefit which has been derived under it. The decided weight of authority in England and America is that no action lies upon the invalid contract, that no decree can be made by a court of equity for its specific performance, nor a recovery be had at law for its breach; but that by proceeding in the proper court, the plaintiff may recover to the extent of the benefit received by the defendant from the execution of the agreement by the plaintiff." Ashbury, etc., Co. v. Riche, L R., 7 H. L. 653; In re Cork, etc., R. Co. L. R., 4 Ch. 748; Garrett v. Kansas City, etc., Co., 113 Mo. 330; Le Warne v. Meyer, 38 Fed. Rep. 191; Nashua, etc., R. Co. v. Boston, etc., R. Co. 164 Mass. 222; Anthony v. Machine Co., 16 R. I. 571; Morville v. Tract Soc., 123 Mass. 129; Northwestern, etc., Co. v. Shaw, 37 Wis. 655; Logan Co., etc., Bank v. Townsend, 139 U. S. 67; Moore v. Tanning Co., 60 Vt. 459.

[2] Day v. Spiral Spring, etc., Co. 57 Mich. 146.

of an immoral nature. The case is not, therefore, one in which the law will leave the parties without redress for the consequences of criminal or immoral action. The plaintiff has a right to sell her manufactures and to be paid for it; the defendant has received something of value from her, and there is manifest equity in its being required to make payment notwithstanding it exceeded its powers in the purchase." Where money is paid on such a contract it may be recovered in an action for money had and received.[1] A corporation which seeks in equity relief against an *ultra vires* contract must return the consideration which it has received.[2]

I. Certain Rules Affecting Doctrine of Ultra Vires.

§ 210. **In general.**—Before proceeding with the discussion of the application of the doctrine of estoppel to *ultra vires* contracts, it is necessary to call attention to certain rules which seem to lie at its very foundation.

§ 211. **Presumption of validity.**—While a corporation must be able to show a grant, express or implied, of power which it seeks to exercise, it is well settled that contracts which are not contrary to the express provisions of the charter are presumed to be within the power of the corporation; and the burden of proof is upon the one denying their validity.[3] Thus, a mortgage executed by the officials of a corporation is presumed to have been executed under proper authority.[4]

§ 212. **Notice of corporate powers.**—The doctrine of *ultra vires* rests largely upon the rule that every person who deals with a corporation must at his peril take notice of the limitations upon its power which are contained in its charter or articles of incorporation. "Every person who enters into a contract

[1] Northwestern, etc., Co. v. Shaw, 37 Wis. 655.

[2] Atlantic, etc., Co. v. Pacific R. Co., 1 Fed. Rep. 745.

[3] Gorder v. Plattsmouth, etc., Co., 36 Neb. 548; Railway Co. v. McCarthy, 96 U. S. 258; Curtis v. Gokey, 68 N. Y. 300; Elkins v. Railroad Co., 36 N. J. Eq. 241; Downing v. Mt. Washington Road Co., 40 N. H. 230; Ex parte Pern, etc., Co., 7 Cow. 540.

[4] Boyce v. Montauk, etc., Co., 37 W. Va. 73.

with a corporation," says Chief Justice Gray,[1] "is bound at his peril to take notice of the legal limits of its capacity, especially where, as in this commonwealth, all acts of incorporation are deemed public acts, and every corporation organized under general laws is required to file in the office of the secretary of the commonwealth a certificate showing the purpose for which the corporation is constituted."

As stated by Chief Justice Waite:[2] "Every corporation necessarily carries its charter wherever it goes, for that is the law of its existence. It may be restricted in the use of some of its powers while doing business away from its corporate home, but every person who deals with it any where is bound to take notice of the provisions which have been made in its charter for the management and control of its affairs, both in life and dissolution." This rule applies to foreign as well as domestic corporations.

It seems rather a harsh rule, however, which requires all persons at their peril to take notice of the provisions of charters which are private acts of which the courts will not take judicial notice.

This doctrine is illustrated by the cases which hold that where a bank loans a corporation more money than the latter's recorded articles of incorporation authorize it to borrow, it does so at its peril, and can collect only the amount which the corporation is thus authorized to contract an indebtedness for.[3]

[1] Davis v. Old Colony R. Co., 131 Mass. 258, 41 Am. Rep. 221. To the same effect see Pearce v. Madison, etc., R. Co., 21 Howard (U. S.) 441; Relfe v. Rundle, 103 U. S. 222; Salt Lake City v. Hollister, 118 U. S. 256; Pittsburgh, etc., R. Co. v. Keokuk, etc., Co., 131 U. S. 371; Central, etc., Co. v. Pullman, etc., Co., 139 U. S. 24; McCormick v. Market Nat. Bank, 165 U. S. 538; Kraniger v. Building Society, 60 Minn. 94; Wilson v. Kings, etc., R. Co., 114 N. Y. 487; Bocock v. Alleghany, etc., Co., 82 Va. 913, 3 Am. St. Rep. 128; Humphrey v. Patrons', etc., Assn., 50 Iowa 607; Elevator Co. v. Memphis, etc., Co., 85 Tenn. 703, 4 Am. St. Rep. 798; Franklin Co. v. Lewiston Inst. for Sav., 68 Me. 43.

[2] Relfe v. Rundle, 103 U. S. 222.

[3] First Nat. Bank v. Kiefer, etc., Co., 95 Ky. 97, 23 S. W. Rep. 675.

§ 213. **Limitations upon the authority of corporate officers.** —Persons who deal with corporations are bound to take notice of the powers of the corporation as contained in the charter and also of the powers of the agents of the corporation. "Persons dealing with the officers of a corporation or with persons assuming to represent it, are chargeable with notice of the purpose of its creation and its powers, and with the authority actual or apparent of its officers or agents, with whom they deal; and when they seek to charge the corporation with liability upon a contract made apparently in its behalf, the burden is upon them to prove the authority of such person assuming to act as such officer or agent, to so make it."[1] This places the requirement of notice of corporate powers and the authority of agents upon the same principle, although in fact they rest upon totally different principles. The former assumes that every person is bound to know the law and the powers of corporations created by law, while the latter rests upon the rule of the law of agency that one who deals with an asserted agent is bound at his peril to know the extent of his authority.[2]

§ 214. **Restrictions contained in by-laws.**—Although there are decisions which say that a person dealing with a corporation is bound to take notice of its *constitution*, *by-laws* and *ways of doing business*,[3] they are contrary to the weight of authority and rest upon no sound principle. There are good reasons for charging all persons with knowledge of what is contained in a public statute or spread upon a public record, but it is difficult to see why they must know the contents of a private rule made by a corporation for the government of its officers and agents in the transaction of its business. The by-laws may, of course, be material as evidence of the actual authority of the agent and are binding upon those who deal with knowledge of their contents.

[1] Wilson v. Kings, etc., R. Co., 114 N. Y. 487; Adriance v. Roome, 52 Barb. (N. Y.) 399. But see § 215, *infra*.

[2] Thompson Corp., § 5974.

[3] Bocock v. Alleghany, etc., Co., 82 Va. 913, 3 Am. St. Rep. 128; Jemison v. Citizens' Bank, 122 N. Y. 135, 19 Am. St. Rep. 482; Bockover v. Life Assn., 77 Va. 85; Relfe v. Rundle, 103 U. S. 222; Haden v. Farmers', etc., Assn., 80 Va. 683. See Nat., etc., Co. v. Home, etc., Bank (Ill.), 54 N. E. Rep. 619.

§ 215. **Limitations upon the general rule.**—The harsh rule which requires a person dealing with corporations to take notice of the extent of their powers is subject to certain well defined limitations. When the want of power is apparent upon an inspection of the charter or statute, the party dealing with the corporation may reasonably be presumed to have knowledge of the defect and the defense of want of authority is available against him. But this defense will not avail against one who can not be presumed to have had knowledge of the want of authority to make the contract. Hence, if the act is apparently within the scope of the corporate powers, and the alleged defect rests upon the existence of certain extrinsic facts peculiarly within the knowledge of the corporate officers, the corporation as against a person dealing in good faith is estopped from denying that which by assuming to make the contract it has virtually affirmed.[1] Thus, a person dealing with a corporation is not bound to know that a power can not be rightfully exercised in a particular case,[2] as that the limit of indebtedness fixed by the charter has been reached.[3] Where an agent has authority to issue negotiable paper for any purpose, a person receiving it in the ordinary course of business is justified in assuming that it was properly issued.[4] So, a holder of negotiable paper issued by a corporation which has power to issue negotiable paper, is not affected by the fact that it was issued at a place and for a purpose not authorized by

[1] Monument Nat. Bank v. Globe Works, 101 Mass. 57; Beecher v. M. & P. Rolling, etc., Co., 45 Mich. 103; Boyce v. Montauk, etc., Co., 37 W. Va. 73; Express Co. v. Railroad Co., 99 U. S. 191; Wardner, etc., Co. v. Jack, 82 Iowa 435; Luttrel v. Martin, 112 N. C. 593; Kennedy v. Savings Bank, 101 Cal. 495. In Bissel v. Railroad Co., 22 N. Y. 258, the court said: "It is a good defense to a corporation when sued upon contract, that in making such contract it exceeded its corporate powers; this defense being allowed, not for the sake of the corporators, but for that of the public. The corporation would, however, be estopped from setting up the defense in a case where the other party to the contract could not be presumed to be cognizant of the excess of power."

[2] Germantown, etc., Co. v. Dhein, 43 Wis. 420, 28 Am. Rep. 549.

[3] Humphrey v. Patrons, etc., Assn., 50 Iowa 607; Auerbach v. LeSeur, etc., Co., 28 Minn. 291; Ellsworth v. St. Louis, etc., Co., 98 N. Y. 553.

[4] Genesee Sav. Bank v. Michigan, etc., Co., 52 Mich. 438; Ellsworth v. St. Louis, etc., Co., 98 N. Y. 553.

the charter.[1] When a corporation has power to purchase property, the vendor without notice is not affected by the fact that it is purchased for an unauthorized purpose.[2] The distinction in such cases is between the possession and the abuse of a power.

II. Estoppel to Assert Defense of Ultra Vires.

§ 216. **General statement.**—The harshness of the strict rule of *ultra vires* is much softened in many cases by the application of other principles of law. From the mass of decisions the rule may be fairly deduced that an *ultra vires* contract is unenforcible except against those persons and corporations who have by participation, acquiescence, retention of benefits or some other act which it would be contrary to justice to disavow, estopped themselves from interposing the defense. It is safe to say that this is the rule which will govern the courts in the great majority of future cases. Thus, if all the stockholders are estopped in a particular case, the contract may be enforced unless possibly when the rights of creditors of the corporation will thereby be prejudiced, or the contract is against public policy or in violation of law. But the reason for the exception fails when the party seeking to assert the estoppel had knowledge of the fact that the contract was *ultra vires*. The limitation exists only for the benefit of those whose rights would be prejudiced by enforcing the strict legal rule. Only those who have been misled can assert the estoppel. "In the application of the doctrine of *ultra vires*," says Judge Folger,[3] "it is to be borne in mind that it has two phases, one where the question is between the corporate body and the stockholders, or between it and its stockholders, and third parties dealing with it, and through it, with them. When the public is concerned to restrain a corporation within the powers given to it by its charter, an assent of all the stockholders to the use of unauthorized

[1] Main v. Casserly, 67 Cal. 127; Lehigh, etc., Co. v. Agricultural Works, 63 Wis. 45; Alexander v. Rollins, 84 Mo. 657.

[2] Thompson v. Lambert, 44 Iowa 239; Cowell v. Springs Co., 100 U. S. 55; Eastern, etc., R. Co. v. Hawkes, 4 H. L. C. 331.

[3] Kent v. Quicksilver, etc., Co., 78 N. Y. 159.

power by the corporate body will be of no avail. When it is a question of the right of a stockholder to restrain the corporate body within its express or incidental powers, the stockholder may in many cases be denied, on the ground of his express assent or his intelligent, though tacit, consent to the corporate action. * * * A corporation may do acts which affect the public to its harm, inasmuch as they are *per se* illegal or *malum prohibitum*. Then no assent of stockholders can validate them. It may do acts not thus illegal, though there is want of power to do them, which affect only the interest of the stockholder. They may be made good by the assent of the stockholders; so that strangers to the stockholders, dealing in good faith with the corporation, will be protected in a reliance upon those acts." It will be observed that according to this rule, there can be no estoppel asserted in aid of the enforcement of a contract which is illegal because *malum in se* or *malum prohibitum*.

§ 217. **Estoppel—Rule of the supreme court.**—The position of the supreme court of the United States in reference to the application of the doctrine of estoppel to *ultra vires* contracts is clearly stated in a very recent case,[1] which grew out of an attempt to hold a national bank liable as a stockholder in another corporation. The bank had power under certain circumstances to become the legal holder of such stock, but in the particular case the act was beyond its power. The case may thus be distinguished from those cases where there is an absolute want of power. But in deciding that the bank could plead the defense of *ultra vires*, Mr. Justice White said: "The transfer of the stock in question to the bank being unauthorized by law, does the fact that under some circumstances the bank might have legally acquired stock in the corporation, estop the bank from setting up the illegality of the transaction? Whatever divergence of opinion may arise on this question from conflicting adjudications in some of the state courts, in this

[1] California Bank v. Kennedy, 167 U. S. 362. This is the doctrine of the English decisions. Ashbury, etc., R. Co. v. Riche, L. R., 7 H. L. 653; Attorney-General v. Great Eastern R. Co., 5 App. Cas. 473; Trevor v. Whitworth, 12 App. Cas. 409; Oregon, etc. Co. v. Roper, 1892 App. Cas. 125.

court it is settled in favor of the right of a corporation to plead its want of power, that is to say, to assert the nullity of an act which is an *ultra vires* act." In another case the court said:[1] "A contract made by a corporation beyond the scope of its powers, express or implied, on a proper construction of its charter, can not be enforced or rendered enforcible by the application of the doctrine of estoppel."

§ 218. **Partially executed ultra vires contracts.**—According to the weight of authority in the state courts where there has been performance of an *ultra vires* contract on the part of the corporation, the other party is estopped to assert the claim that the corporation had no authority to make the contract.[2] "One who has received from a corporation the full consideration of his engagement to pay money * * * can not avail himself of the objection that the contract thus fully performed by the corporation was *ultra vires* and not within its chartered privileges and powers."[3] The converse of this rule that a private corporation can not avail itself of the defense of *ultra vires*, where the contract has been in good faith fully performed by the other party and the corporation has had the benefit of the contract and the performance, is supported by the overwhelming weight of authority,[4] although it has been

[1] Union, etc., R. Co. v. Chicago, etc., R. Co., 163 U. S. 564.

[2] Linkauf v. Lombard, 137 N. Y. 417; Oil Creek, etc., R. Co. v. Pennsylvania, etc., Co., 83 Pa. St. 160; Reynolds v. Crawfordsville Bank, 112 U. S. 405; Shewalter v. Pirner, 55 Mo. 218; Eckman v. Chicago, etc., R. Co., 169 Ill. 312; Chester, etc., Co. v. Dewey, 16 Mass. 94; Germantown, etc., Co. v. Dhein, 43 Wis. 420; Whitney, etc., Co. v. Barlow, 63 N. Y. 62; Bissell v. Michigan, etc., R. Co., 22 N. Y. 258; Building Assn. v. Lampson, 60 Minn. 422; Bath, etc., Co. v. Claffy, 151 N. Y. 24; Carson City, etc., Bank v. Carson City, etc. Co., 90 Mich. 550; National Bank v. Whitney, 103 U. S. 99. In Alabama, the defense of *ultra vires* may be interposed without accounting for benefits received.

[3] Whitney, etc., Co. v. Barlow, *supra*.

[4] Darst v. Gale, 83 Ill. 136; Bradley v. Ballard, 55 Ill. 413, 8 Am. Rep. 656; Kadish v. Loan Assn., 151 Ill. 531; Bissell v. Michigan, etc., R. Co., 22 N. Y. 258; Peoria, etc., R. Co. v. Thompson, 103 Ill. 187; Manchester, etc., R. Co. v. Concord, etc., R. Co., 66 N. H. 100, 20 Atl. Rep. 383; Camden, etc., R. Co. v. Mays, etc., R. Co., 48 N. J. L. 530; In re Pendleton, etc., Co., 24 Ore. 330; Seymour v. Guaranty, etc., Soc., 54 Minn. 147; Holmes, etc., Co. v. Holmes, etc., Co., 127 N. Y. 252; Rider, etc., Co. v. Roach, 97 N.

subjected to some criticism.[1] There are decisions, however, which hold that the defense can be interposed at any time by either party.[2] But this rule should evidently apply only to contracts which are contrary to public policy or positive law. The part performance must be such as will render the defense of *ultra vires* unjust and inequitable.[3] An *ultra vires* contract wholly executory will never be enforced.

§ 219. **Estoppel—Retention of benefits.**—The effect of part performance is generally made to turn upon the fact that by reason thereof the other party has received and retains benefits under the contract. Hence, neither party to an *ultra vires* contract will be heard to say that one or both of the parties thereto had no power to make the contract while he retains the benefits received under the contract.[4] The result is that the

Y. 378; State Board v. Citizens', etc., R. Co., 47 Ind. 407, 17 Am. Rep. 702; Connecticut, etc., Bank v. Fiske, 60 N. H. 363; Wood v. Corry, etc., Wks., 44 Fed. Rep. 146, 12 L. R. A. 168; Carson City, etc., Bank v. Carson City, etc., Co., 90 Mich. 550, 30 Am. St. Rep. 454; Wright v. Pipe Line Co., 101 Pa. St. 204, 47 Am. Rep. 701; Wright v. Hughes, 119 Ind. 324, 12 Am. St. Rep. 412; Main v. Casserly, 67 Cal. 127.

[1] Taylor Priv. Corps., § 279.

[2] The following cases hold that the corporation may defend on the ground of *ultra vires* although it has enjoyed and retains the benefits of the contract. Albert v. Savings Bank, 1 Md. Ch. 407; Sherwood v. Alvis, 83 Ala. 115, 3 Am. St. Rep. 695; Chewacla, etc., Wks. v. Dismukes, 87 Ala. 344. See Boynton v. Lynn, etc., Co., 124 Mass. 197.

[3] Nassau Bank v. Jones, 95 N. Y. 115; Bosshardt, etc., Co. v. Crescent, etc., Co., 171 Pa. St. 109.

[4] Seymour v. Spring Forest, etc., Assn., 144 N. Y. 333, 26 L. R. A. 859; Bath, etc., Co. v Claffy, 151 N. Y. 24, 36 L. R. A. 664; Wright v. Hughes, 119 Ind. 324, 12 Am. St. Rep. 412; Wright v. Pipe Line Co., 101 Pa. St. 204; Hardware Co. v. Phalen, 128 Pa. St. 110; Dewey v. Toledo, etc., R. Co., 91 Mich. 351; Carson City, etc., Bank v. Carson City, etc., Co., 90 Mich. 550; Union, etc., Co. v. Plum, etc., Co., 58 Conn. 219; Louisville, etc., R. Co. v. Flannagan, 113 Ind. 488, 3 Am. St. Rep. 674; Manchester, etc., R. Co. v. Concord R. Co., 66 N. H. 100, 20 Atl. Rep. 383; Colorado, etc., Co. v. Grand Valley, etc., Co. (Colo.), 32 Pac. Rep. 178; Tyler v. Tualatin Academy, 14 Ore. 485; Natchez v. Mallery, 54 Miss. 499; Humphrey v. Patrons', etc., Assn., 50 Iowa 607; Twiss v. Guaranty, etc., Assn., 87 Iowa 733, 55 N. W. Rep. 89; Darst v. Gale, 83 Ill. 136; Wood v. Corry Water Works, 44 Fed. Rep. 146; Linkauf v. Lombard, 137 N. Y. 417; Whitney, etc., Co. v. Barlow, 63 N. Y. 62; Camden, etc., R. Co. v. Mays, etc., R. Co., 48 N. J. L. 530; Sherman, etc., Co. v. Morris, 43 Kan. 282; McGee v. Pacific, etc., Co., 98 Cal. 678; Comw. v. Suffolk, etc., Co., 161 Mass. 550, 37 N. E. Rep. 757; Hitchcock v. Galveston, 96 U. S. 341.

action is maintained *on the contract*, because the party who retains the benefits under it is not permitted to say that it is invalid.[1] "The contract in such case is assumed by the court to be valid, the party seeking to avoid it not being permitted to attack its character in this respect.[2] This rule has been applied where an insurance company issued a policy against loss caused by hail;[3] where a corporation, engaged in the business of innkeeper, sought to escape liability as such to a guest,[4] and where a street railway corporation agreed to pay a certain sum if an agricultural fair was held at a certain place, and attempted to avoid payment on the ground that the contract was *ultra vires*."[5] "There are few rules," said Chief Justice Gilfillan,[6] "better settled or more strongly supported by authority, with fewer exceptions in this country, than that when a contract by a private corporation, which is otherwise unobjectionable, has been performed on one side, the party which has received and retains the benefit of such performance shall not be permitted to evade performance on the ground that the contract was in excess of the purpose for which the company was created. The rule may not be strictly logical, but it prevents a great deal of injustice." Thus, a party who has borrowed money from a corporation and given his promissory note therefor can not, when sued upon the note, be heard to say that the corporation had no power to make the loan.[7] In a very recent Wisconsin case, where a receiver of a foreign

[1] Wright v. Pipe Line Co., 101 Pa. St. 204; Dewey v. Railroad Co., 91 Mich. 351.

[2] Denver, etc., Co. v. McClelland, 9 Colo. 11.

[3] Denver, etc., Co. v. McClelland, 9 Colo. 11.

[4] Magee v. Improvement Co., 98 Cal. 678.

[5] State Board v. Citizens', etc., R. Co., 17 Ind. 407.

[6] Seymour v. Guaranty, etc., Society, 54 Minn. 147.

[7] Poock v. Lafayette, etc., Assn., 71 Ind. 357. In Steam Nav. Co. v. Weed, 17 Barb. 378, Parker, J., said: "It ill becomes the defendants to borrow from the plaintiffs $1,000 for a single day, to relieve their immediate necessities, and then to turn around and say: 'I will not return you this money, because you had no power, by your charter, to lend it.' Let them first restore the money, and then it will be time enough for them to discuss with the sovereign power of the state of Connecticut the extent of the plaintiff's chartered privileges. We shall lose our respect for the law, when it so far loses its character for justice as

corporation asserted that the action of the officers of the corporation in depositing securities in the state in order to qualify the corporation for doing business there was *ultra vires*, the court said: "It is well settled that a corporation can not avail itself of the defense of *ultra vires* when the contract in question has been in good faith, fully performed by the other party and the corporation has had the full benefit of the performance of the contract. Much less will the claim that the transaction was *ultra vires* be allowed as a ground for rescinding the contract and restoring to the complaining party on that ground the property or funds, with which he has parted, after he has had the benefit of full performance of the contract by the other party; and, in general, the plea of *ultra vires* will not be allowed to prevail, whether interposed for or against a corporation, when it will not advance justice, but, on the contrary, will accomplish a legal wrong."[1]

§ 220. **Acquiescence in ultra vires acts.**—If a stockholder desires protection against an *ultra vires* act of the corporation he must act promptly and energetically, or he will be bound by acquiescence. If he assents to the transaction or for an unreasonable time acquiesces until the other party has acted on the faith of the transaction so that he will suffer great injury by its repudiation, a court of equity will be slow in granting him relief.[2]

to sanction the defense here attempted."

[1] Lewis v. American, etc., Assn., 98 Wis. 203, 73 N. W. Rep. 793, 39 L. R. A. 559, citing Kadish v. Garden, etc., Assn., 151 Ill. 531; Whitney, etc., Co. v. Barlow, 63 N. Y. 62; Union, etc., Bank v. Matthews, 98 U. S. 621; Carson City, etc., Bank v. Carson City, etc., R. Co., 90 Mich. 550, 30 Am. St. Rep. 454. As to the right of the receiver to assert the defense of *ultra vires*, see Abbott v. Baltimore, etc., Co., 1 Md. Ch. 542; First, etc., Bank v. Kiefer Co., 95 Ky. 97.

[2] Stewart v. Transportation Co., 17 Minn. 372 (Gil. 348); Alexander v. Searcy, 81 Ga. 536; Dimpfel v. Railroad Co., 110 U. S. 209; St. Louis, etc., R. Co. v. Terre Haute, etc., R. Co., 145 U. S. 393; Boyce v. Montauk, etc., Co., 37 W. Va. 73; Ashhurst's Appeal, 60 Pa. St. 290; Green's Brice's Ultra Vires, 783. In Nashua, etc., Corp. v. Boston, etc., Corp., 157 Mass. 268, 31 N. E. Rep. 1060, it was held that a contract for the joint operation of two railroads would not be declared *ultra vires* in an action on the contract, when the defense was not set up in the answer, or

It is said to be the continuing duty of a party to an *ultra vires* contract to rescind the same, but where a suit was brought to have set aside and canceled a conveyance of the plaintiff's railroad and franchises, plaintiff failed because of his laches.

It appeared that the contract had been fully executed on the part of the plaintiff by the actual transfer of its railroad and franchises to the defendant and that the defendant had held the property, and paid the stipulated consideration from time to time for a period of seventeen years, and had taken no steps to rescind or repudiate the contract. The contract was held to be *ultra vires*, but the court said:[1] "Upon this state of facts, for the reasons above stated, the plaintiff considered as a party to the unlawful contract has no right to invoke the assistance of a court of equity to set it aside. And so far as the plaintiff corporation can be considered as representing the stockholders, and seeking to protect their interests, it and they are barred by laches."[2] This case is not like those in which the defendant, having abandoned or refused to perform the unlawful contract, has been held liable to the plaintiff, as upon an implied contract, for the value of what he has received from him, and had no right to retain.[3]

§ 221. **Ratification of ultra vires acts.**—A corporation may ratify a contract which it has power to make. Hence, if a contract is entered into by some one in its behalf without authority, or is voidable because some formality has not been observed, it may be ratified by the corporation acting in some proper form.[4] A voidable contract may be ratified by a majority of the stockholders, because a majority having the con-

in a previous action between the same parties on the same contract, and when no statute or decision of that state or of the foreign state is cited in support of the defense, and when there is nothing to show that the legislature or any public officer of either state has ever objected to the contract.

[1] St. Louis, etc., R. Co. v. Terre Haute, etc., R. Co., 145 U. S. 393.

[2] Harwood v. Railway, 17 Wall. (U. S.) 78.

[3] Spring Co. v. Knowlton, 103 U. S. 49; Bank v. Townsend, 139 U. S. 67

[4] North Point, etc., Co. v. Utah, etc., Co., 16 Utah 246, 40 L. R. A. 851; Seymour v. Spring Forest, etc., Assn., 144 N. Y. 333, 26 L. R. A. 859.

trol of the corporation within the general scope of its powers might have made the original contract. But a contract which is *ultra vires* because in excess of the power of the corporation can not be ratified.[1] The question of the liability of a corporation for the torts of its agents in excess of their authority will be considered elsewhere. The corporation may become responsible for such acts by receiving the benefits accruing therefrom. Thus, where the agents of a corporation organized for educational purposes engaged in the business of conveying passengers from the railway station to the grounds of its school buildings, it was held that the corporation was liable for injuries occasioned by the negligence of such agents where it appeared that the managing officers knew that the business was being carried on and received and retained the income resulting therefrom.[2]

III. Contracts Illegal Because Malum Prohibitum or Malum In Se.

§ 222. **General statement.**—Attention has already been called to the distinction sometimes made between contracts which are merely unauthorized by the corporate charter and contracts which are illegal because contrary to law. The word illegal is very often used to characterize both kinds of contracts. A contract may be illegal because immoral in itself, because expressly forbidden by statute, or because it is against public policy. An act which is not authorized is *ultra vires;* an act which is not only not authorized, but expressly prohibited is not only *ultra vires* but also illegal. There is no reason for using the phrase *ultra vires* to describe contracts which are illegal in this sense of the word, because they are governed by

[1] San Diego, etc., R. Co. v. Pacific, etc., Co., 112 Cal. 53, 33 L. R. A. 788.

[2] Nims v. Mt. Hermon, etc., School, 160 Mass. 177, 22 L. R. A. 364; Eastern, etc., R. Co. v. Broom, 6 Exch. 314. "He that receiveth a trespasser, and agreeth to a trespass after it is done, is no trespasser, unless the trespass was done to his use or for his benefit, and then his subsequent agreement amounteth to a commandment." 4 Inst. 317.

the same principles that govern similar contracts between individuals.[1]

§ 223. **Contracts malum in se.**—There is nothing peculiar to the law of corporations in contracts of this character. Such contracts can never be enforced. The illegality, however, must adhere in the contract itself, and mere knowledge on the part of one party that the proceeds of the contract will be used for an illegal purpose will not render the contract void as against the party who did not participate in the illegal undertaking.[2] An illustration of contracts which are illegal, *malum in se*, is found in an agreement to pay for lobbying an act through the state legislature.[3]

§ 224. **Contracts against public policy.**—Certain classes of contracts, while not expressly prohibited by statute, are regarded as illegal, because against the public policy of the state. Corporations which are charged with public duties are not permitted to enter into contracts which will render them incapable of performing such duties. All such contracts on grounds of public policy are illegal and unenforcible. Thus, such corporations can not, without the consent of the state, dispose of their entire property, transfer or encumber their franchises, or make any contracts which will deprive them of the ability to perform their public duties.[4] *Ultra vires* contracts of this character, which relate to franchises, trust monopolies, traffic and pooling arrangements, have been already considered.[5]

§ 225. **Statutory prohibitions.**—If the statute expressly prohibits the making of a certain contract and uses language which shows that it was the intention of the legislature that

[1] See § 201, *supra*.

[2] Tracy v. Talmage, 14 N. Y. 162; Jones v. Planters' Bank, 9 Heisk. (Tenn.) 455.

[3] Marshall v. Baltimore, etc., R. Co., 16 How. (U. S.) 314.

[4] American, etc., Co. v. Union Pac. R. Co., 1 McCray 188; Visalia, etc., Co. v. Sims, 104 Cal. 326. See cases cited, § 125, *supra*. A mortgage covering the corporate property and franchises may be valid as to the property and invalid as to the franchises. Gloniger v. RailroadCo., 139 Pa. St. 13.

[5] § 176, *supra*.

such contracts should be void, they are necessarily illegal and unenforcible. In many states there are statutory provisions, which prohibit corporations from doing any acts not authorized by their charters. Thus, the New York statute[1] provides that "In addition to the powers enumerated in the first section of this recital, and to those expressly given in its charter, or the act under which it is or shall be incorporated, no corporation shall possess or exercise any corporate powers, except such as shall be necessary to the exercise of powers so enumerated and given." This is merely a statement of the common law rule which has already been discussed. A contract in excess of the corporate power is no more illegal in the proper use of that word, than it would be if no such statute existed. It is merely *ultra vires* for want of corporate power. The *quality* of the act is in no way determined by the statute. The New York courts construe the provision as merely declaratory of the common law,[2] although in other states such a statute is regarded as making the act illegal and void.[3] The English courts under the theory of general capacity are in exactly the same position as an American court under such a statute. Under the doctrine of general capacity the charter contains only prohibitions, and what is not prohibited, if within the scope of the object of the incorporation, is granted.[4] Under general statutes like that above quoted, every act not granted is prohibited with the same force as by negations contained in English corporate charters.

As a general proposition it may be said that a prohibited act is an illegal act, and an illegal act can not be made the basis of a legal action. In this respect it is like an act *malum in se*, which involves moral turpitude, and is governed by the maxim *ex turpi causa non oritur actio*. But this general

[1] 3 N. Y. Rev. Stat. (8th ed.) 1723.

[2] Curtis v. Leavitt, 15 N. Y. 9; Bond v. Terrell, etc., Co., 82 Tex. 309.

[3] Morris, etc., R. Co. v. Sussex, etc., R. Co., 20 N. J. Eq. 542.

[4] East, etc., Co. v. Eastern, etc., R. Co., 11 C. B. 775. All *ultra vires* acts are generally called illegal. See Taylor v. Chichester, etc., R. Co., L. R. 2 Ex. 356; South Yorkshire R. Co. v. Great Northern R. Co., 9 Ex. 55, 84; Scottish, etc., R. Co. v. Stewart, 3 Macq. 382, 415. See Nat., etc., Co. v. Home Sav. Bank (Ill.), 54 N. E. Rep. 619.

rule is subject to exceptions. "If a statute expressly forbids a corporation to make a certain contract, the contract is void, even though not expressly declared to be so, and is incapable of ratification; and that the contract is unlawful may be pleaded by any one to an action founded directly and exclusively on the contract;[1] unless (1) the statute expressly states what the consequences of violating it shall be and those consequences are other than that the contract is void;[2] or (2) the statutory prohibition was evidently imposed for the protection of a certain class of persons who alone may take advantage of it; or (3) to adjudge the contract void and incapable of forming a basis of a right of action would clearly frustrate the evident purpose of the prohibition itself."[3]

§ 226. **Illustrations.**—The most of the cases in which the courts enforce a contract, although made in the face of charter or statutory prohibition, fall under the third exception to the general rule stated in the preceding section. Where a national bank made an *ultra vires* loan of money upon real estate security, the court refused to enjoin the sale of the security under a deed of trust, as it was not the intention of the law "that stockholders and perhaps depositors and other creditors should be punished and the borrower rewarded by giving success to this defense whenever the offensive facts should occur. The impending danger of a judgment of ouster and dissolution was, we think, the check and none other contemplated by congress. That has been always the punishment prescribed for the wanton violation of a charter, and it may be made to follow whenever the proper public authority shall see fit to invoke its application."[4] An act which provides that savings banks shall not make loans upon personal security alone will not prevent the bank from maintaining an action for a note given for such prohibited loan.[5]

[1] Bank v. Owens, 2 Pet. (U. S.) 527; Leavitt v. Palmer, 3 N. Y. 19; Bank v. Alvord, 31 N. Y. 473.

[2] Pratt v. Short, 79 N. Y. 437.

[3] Taylor Priv. Corp., § 297.

[4] National Bank v. Matthews, 98 U. S. 621; National Bank v. Whitney, 103 U. S. 99.

[5] Farmington Sav. Bank v. Falls, 71 Me. 49.

A violation of the law which forbids national banks to loan more than a certain amount to one person will not prevent the enforcement of such an excessive loan.[1] So, a director who borrows from the bank in violation of the statute, may be compelled to repay the money.[2] The same rule applies when the prohibition arises by implication, as where national banks are impliedly forbidden to take real estate security, for loans.[3] So, but for other reasons, a statutory prohibition of a debt will not authorize a corporation to keep money which it was forbidden to borrow.[4]

§ 227. **Liability for benefits received under illegal contracts.** —It has already been stated that under contracts *ultra vires* for want of power, the defense can not be asserted while benefits received thereunder are retained.[5] Where the contract is illegal, *malum per se*, the parties being *particeps criminis*, the court will leave them where it found them. If it is merely *malum prohibitum*, it is held in some cases that it may be rescinded at any time and the money advanced thereon recovered.[6] Where both parties to such a contract have received benefits under it, the one which seeks to rescind and recover what he has paid must offer to return what he has received.[7] So, the party who is less guilty than the other may disaffirm and recover what he has parted with. The statutory prohibition may be intended for the benefit of the party seeking relief. Thus, where a bank issued bills contrary to law, the court said:[8] "The corporation issuing bills contrary to law and against penal sanctions is deemed more guilty than the members of the community who receive them, whenever the receiving of them is not expressly prohibited. The latter are regarded

[1] National Bank v. Matthews, 98 U. S. 621.

[2] Lester v. Howard Bank, 33 Md 558.

[3] National Bank v. Matthews, 98 U. S. 621.

[4] Conn., etc., Bank v. Fiske, 60 N. H. 363.

[5] Franco, etc., Co. v. McCormick, 85 Tex. 416. *Contra* (Ill.), 54 N. W. Rep. 619.

[6] Spring Co. v. Knowlton, 103 U. S. 49; Oneida Bank v. Ontario Bank, 21 N. Y. 490.

[7] American, etc., Co. v. Union, etc., R. Co., 1 McCrary 188.

[8] Thomas v. Richmond, 12 Wall. 349; White v. Bank, 22 Pick. 181, , Tracy v. Talmage, 14 N. Y. 162,

as the persons intended to be protected by the law; and, if they have not themselves violated an express law in receiving the bills, the principles of justice require that they should be able to recover the money received by the bank for them."

IV. Irregular Exercise of Power

§ 228. **Effect of irregularities.**—There remains for consideration the case of an irregular exercise of an authorized power. It is apparent that a contract of this character should not be held void. Generally contracts which are within the general scope of the corporate powers, but in excess of the powers in some particulars, are valid, unless they are contrary to public policy. Persons dealing with the corporation are not required to take notice of the failure to observe formalities or of extrinsic facts which are within the knowledge of the corporation.[1]

When a corporation has acted upon an executed contract, it is to be presumed against it that everything necessary to make it a binding contract on both parties was done, the corporation having had all the advantage it would have had if the contract had been regularly made.[2]

§ 229. **Want of power and neglect of formalities.**—The manner of executing a power may be prescribed by the statute in such manner as to be a limitation upon the grant, and to render an act done in any other way voidable.[3] But when the general power to do an act exists persons dealing with a corporation may assume that the necessary formalities have been observed in its exercise.[4] As said by one court:[5] "If a corporation in the exercise of a franchise not granted to it by the legislature makes a contract or does an act, they may plead their want of authority on the ground that the courts will not interfere to grant redress between two persons engaged in an

[1] The leading case is probably, Moore v. Mayor, etc., 73 N. Y. 238, 29 Am. Rep. 134; Insurance Co. v. Dhein, 43 Wis. 420; Merchants' Bank v. State Bank, 10 Wall. (U. S.) 604.

[2] Rule in 7 Eng. Rul. Cas. 353.

[3] See Gutta Percha, etc., Co. v. Ogallalo, 40 Neb. 775.

[4] Miners', etc., Co. v. Zellerbach, 37 Cal. 543, 99 Am. Dec. 300.

[5] City, etc., Co. v. Carrugi, 41 Ga. 660.

illegal enterprise. But if the contract is within the scope of the franchise, but fails to conform to the regulations prescribed by the charter for the guidance of its officers, and the protection of the rights of the members as to each other, the corporation may be held liable under the general rules of law, as to agency, estoppel and waiver." The question often arises where services have been rendered under a contract not made in accordance with statutory requirements. Thus, one who is employed to teach a district school, may recover for services actually rendered, although the contract of employment was not authorized by the trustees at a meeting of all their number called for that purpose as required by law. The court said:[1] "Having availed itself of the services, and received the benefits, it is bound in conscience to pay, and will not be heard to say that the original agreement was not made by a person legally authorized to make it." Another illustration is found in the rule that negotiable paper issued by a corporation for an unauthorized purpose is valid in the hands of an innocent holder if the corporation had power to issue such paper for any purpose.

§ 230. **Reasons for the distinction—Statement of Chief Justice Sawyer.**—The distinction between acts which are beyond the power of the corporation and acts within the general scope of the corporate power, but in excess thereof in some particular, is thus stated by the supreme court of California:[2]

[1] Fister v. La Rue, 15 Barb. (N. Y.) 323. See, also, City of Ellsworth v. Rossiter, 46 Kan. 237; Cincinnati v. Cameron, 33 Ohio St. 336; Pixley v. Railroad Co., 33 Cal. 183; Ward v. Forest Grove, 20 Ore. 355; Hawk v. Marion County, 48 Iowa 472; Kneeland v. Gilman, 24 Wis. 39. In Commissioners v. Webb, 47 Kan. 104, the court said: "Where a corporation, municipal or otherwise, has received benefits from others, upon contracts *ultra vires* or void because of some irregularity or want of power in their creation, but not void because made in violation of express law, or good morals, or public policy, and where the corporation retains such benefits, it must pay for them." But a school teacher can not recover for services rendered when he had not the certificate of qualifications required by statute. It was treated as a prohibitory statute. Goose River Bank v. Willow Lake School Tp., 1 N. Dak. 26, 26 Am. St. Rep. 605.

[2] Miners', etc., Co. v. Zellerbach, 37 Cal. 543. For the same principle

"Strangers are presumed to know the law of the land, and they are bound when dealing with corporations to know the powers conferred by the charters. These are open to their inspection and it is easy to determine whether the act is within the scope of the general powers conferred for that purpose. But they have no access to the private papers of the corporation or to the motives which govern directors or stockholders, and no means of knowing the purposes for which an act that may be lawful for some purposes is done. The very fact that the appointive officers of the corporation assume to do an act in the apparent performance of their duties, which they are authorized to perform for the lawful purposes of the corporation is a representation to those dealing with them that the act performed is for a lawful purpose. And such is the presumption of the law, and upon this presumption, strangers having no notice in fact of the unlawful purpose are entitled to rely. * * Upon any other principles there would be no safety in dealing with corporations, and the business operations of these institutions would be greatly crippled, while the interests of the stockholders and the public and their general usefulness would be seriously impaired. The officers are appointed by the corporation, and if any loss results to strangers dealing with the corporation in matters within the general scope of their duties, it should fall upon the corporation which is responsible for their appointment rather than upon parties who have no other means of ascertaining the facts and must rely upon their assurances or not deal with the corporation at all."

as determining the liability of a public corporation for torts, see Sacks v. City of Minneapolis (Minn., 1898), 77 N.W. Rep. 563.

CHAPTER 10.

LIABILITY FOR TORTS AND CRIMES.

§ 232. General statement.
233. Growth of the law.
234. The modern rule.
235. Liability for punitive damages.
236. The commission of crime.
237. Crimes involving intent.
238. Contempt of court.
239. Proceedings.

§ 232. **General statement.**—The rule by which corporations are held responsible for the results of their tortious acts has been established in the face of much opposition. In the earlier cases the courts became entangled in the meshes of metaphysical theories regarding the nature of corporations and wasted much thought in trying to ascertain how an incorporeal entity without conscience or soul could entertain the intent which was an essential element of certain torts and crimes. It was said that a corporation could exercise only such powers as were expressly or by implication conferred upon it by its charter and no charter conferred the authority to commit a tort or a crime. Hence when the agents of a corporation were guilty of a wrong they were to be considered as acting in their individual capacity and as individuals be held responsible for their acts. So it was said that indictment required an appearance at the bar, and an incorporeal entity could not appear, from which it was supposed to follow that a corporation could not be indicted for a crime. But it gradually dawned upon the courts that if "the invisible, intangible essence of air, which we term a corporation, can level mountains, fill up valleys, lay down iron tracks and run railroad cars upon them, it can intend to do it, and can act therein as well viciously as virtuously.[1]

[1] Bishop New Crim. Law, § 417.

§ 233. **Growth of the law.**—It was long thought that as a corporation had no mouth with which to utter slander, or hand with which to write libels or commit batteries, or mind to suggest malicious prosecutions or other wrongs—as it was an artificial person, and could speak and act only through the agency of others—it was not liable for any torts except such as resulted from some act of commission or omission of its agents or servants while acting within the scope of granted powers, or wrongfully omitting and neglecting some duty imposed by its charter or by-laws. Consequently it was necessary to allege that the act committed was done while acting within the scope and power of the company, or that the act omitted was required to be performed. Whether it were wise to depart from this rule that excepted corporations from liability for the acts of its agents in cases where the character of the act depended upon motives or intent seems no longer open. The old idea that, because a corporation had no soul, it could not commit torts, or be the subject of punishment for tortious acts, may now be regarded as obsolete. The rights, the powers and the duties of corporate bodies have been so enlarged in modern times, and they have become so numerous, and enter so largely into the every-day transactions of life, that it has become the policy of the law to subject them, so far as practicable, to the same civil liability for wrongful acts as attach to natural persons. The liability is not restricted to acts committed within the scope of granted powers, but the corporation may be liable in an action for false imprisonment, malicious prosecution or libel.[1]

[1] For a statement of the reasons for the rule that a corporation is not liable for a malicious prosecution, see Abrath v. Northeastern R. Co., 11 Q. B. Div. 440 (1883), 25 Am. L. Reg. 759, per Lord Brammell. The American cases holding this doctrine have been overruled. In Reed v. Home Sav. Bank, 130 Mass. 443, the modern doctrine was stated and the court said: "If a corporation be the intangible being it is asserted to be, a greater and more mischievous monster can not be imagined. According to the doctrine contended for, if they do and act within the scope of their corporate powers, it is legal and they are not amenable for it. If the act be not within the scope of their legitimate powers, they had no right to do it; it was not one of the objects for which they were incorporated, and therefore it is no act of the

§ 234. **The modern rule.**[1]—It is now the settled law that a corporation is liable *civiliter* for torts committed by its agents or servants precisely as a natural person, and that it is liable as a natural person for the acts of agents done by its authority, express or implied, although there is neither a written appointment under seal, nor a vote of the corporation constituting the agency or authorizing the act.[2] When an officer does an act which is within the general scope of his powers, although circumstances may exist which render the particular act a violation of his duty, the corporation is nevertheless bound by his acts as to persons dealing in ignorance of those circumstances, and is responsible to innocent third parties who have sustained damages occasioned by such acts.[3] But in a late case it was said: "In consequence, however, of the fact that a corporation must of necessity act through its agents, courts have almost invariably held that to hold a corporation liable for a tortious act committed by its agent the act must be done by its express precedent authority, or ratified and adopted by the corporation. Nor is a corporation responsible for unauthorized and unlawful acts, even of its officers, though done *colore officii*. To fix the liability it must either appear that the officers were expressly authorized to do the act or that it was done bona fide

corporation at all. This doctrine leads to the absolute immunity for every species of wrong, and can never be sanctioned by any court of justice." See Orr v. U. S Bank, 1 Ohio 36, 13 Am. Dec. 588.

[1] An exception to the modern rule still exists,—a public charitable corporation is not liable for the torts of its agents. See Fire Ins. Patrol v. Boyd, 120 Pa. St. 624, 6 Am. St. R. 745, Wilgus' Cases and cases there cited; assault and battery, Eastern, etc., R. Co. v. Broom, 6 Ex. (Wels. H. & G.) 314, Wilgus' Cases; false imprisonment, Wheeler & Wilson Mfg. Co. v. Boyce, 36 Kan. 350, 59 Am. R. 571, Wilgus' Cases; slander and libel, Behre v. National, etc., Co., 100 Ga. 213, Wilgus' Cases.

[2] Denver, etc., R. Co. v. Harris, 122 U. S. 597, per Mr. Justice Harlan; Railroad Co. v. Quigley, 21 How. 202; Salt Lake City v. Hollister, 118 U. S. 256; Steamboat Co. v. Brockett, 121 U. S. 637; Bank v. Graham, 100 U. S. 699; Fitzgerald v. Fitzgerald, etc., Co., 41 Neb. 374, 59 N. W. Rep. 838; Miller v. Railroad Co., 8 Neb. 219; State v. Morris, etc., R. Co., 23 N. J. 360; Wachsmuth v. Merchants' Nat, Bank, 96 Mich. 426; Randall v. Evening News, 97 Mich. 136; Railroad Co. v. Schuyler, 34 N. Y. 30; Kansas City, etc., Co. v. Phillips, 98 Ala. 159; Bank v. Butchers', etc., Bank, 16 N. Y. 125; Bissell v. Railroad Co., 22 N. Y. 258; Bank v. Patchin Bank, 13 N. Y. 309; Williams v. Planters' Ins. Co., 57 Miss. 759; New York, etc., R. Co. v. Haring, 47 N. J. L. 137; Gunn v. Railroad Co., 74 Ga. 509; Yarborough v. Bank of England, 16 East 6; Lake Shore R. Co. v. Prentice, 147 U.S. 101; Chestnut Hill, etc., Co. v. Rutter, 4 S. & R. (Pa.) 6, 8 Am. Dec. 675; Hussey v. Norfolk, etc., R. Co., 98 N. C. 34, 2 Am. St. Rep. 312; Goodspeed v. Bank, 22 Conn. 530.

[3] Carter v. Howe, etc., Co., 51 Md. 290, 34 Am. Rep. 311.

in pursuance of a general authority in relation to the subject of it, or that the act was adopted or ratified by it."[1] The liability of a corporation for the consequences of acts of its officers, done within the scope of their general powers, is not affected by the fact that the act which the officers have assumed to do is one which the corporation itself could not rightfully do. A corporation, like an individual, may do wrong through its agent[2] and be liable for the wrongful act.[3] The liability extends to torts involving a specific intent, or the element of malice, as fraud,[4] malicious wrongs,[5] libel,[6] malicious prosecution[7] or conspiracy.[8]

§ 235. **Liability for punitive damages.**—Out of the supposed inability of a corporation to entertain an evil intent has grown the contention over the question of its liability for exemplary or punitive damages. As a general rule such damages can not be allowed against a master for the mere negligence of his servants, however gross, if he is personally free from fault. But the rule is subject to qualification when the master is a

[1] Central R. Co. v. Brewer, 78 Md. 394, 27 L. R. A. 63.

[2] Booth v. Bank, 50 N. Y. 396; Nims v. Mt. Hermon Boys' School, 160 Mass. 177, 22 L. R. A. 364; Wheeler, etc., Co. v. Boyce, 36 Kan. 350. As to the liability of municipal corporations for the tortious acts of its officers see Salt Lake City v. Hollister, 118 U. S. 256.

[3] Vanderbilt v. Richmond, etc., Co., 2 N. Y. 479, 51 Am. Dec. 315; Green v. Omnibus Co., 7 C. B. (N. S.) 290; Jaggard Torts, p. 168. That an action for deceit will lie against a corporation, see Dorsey, etc., Co. v. McCaffery, 139 Ind. 545; Nash v. Minnesota, etc., Co., 163 Mass. 574; Bosley v. National, etc., Co., 123 N. Y. 550; Erie City Iron Works v. Barber & Co., 106 Pa. St. 125; Mackay v. Bank of New Brunswick, 5 P. C. 391.

[4] Abrath v. North Eastern R. Co., L. R. 11 App. 247.

[5] Goodspeed v. East Haddam Bank, 22 Conn. 530; Green v. London, etc., Co., 7 C. B. N. S. 290; Fogg v. Boston, etc., R. Co., 148 Mass. 513, 12 Am. St. Rep. 583; Aldrich v. Press Printing Co., 9 Minn. 133, Gil. 123, 86 Am. Dec. 84; Hussey v. Norfolk, etc., R. Co., 98 N. C. 34, 2 Am. St. Rep. 312.

[6] Fogg v. Boston, etc., R. Co., *supra*; Missouri, etc., R. Co. v. Richmond, 73 Tex. 568, 15 Am. St. Rep. 794. A corporation can not, probably, be held for slander, in the absence of a statute. See Townsend Slander and L., § 265. But there are *dicta* to the contrary. See Hussey v. Norfolk, etc., R. Co., 98 N. C. 34, 2 Am. St. Rep. 312. But see Behre v. National, etc., Co., 100 Ga. 213, 62 Am. St. R. 320, 27 S. E. Rep. 986, Wilgus' Cases; also Reddit v. Singer Mfg. Co., 32 S. E. Rep. (N. C.) 392.

[7] Reed v. Home Sav. Bank, 130 Mass. 443, 39 Am. Rep. 468; Indiana, etc., Co v. Willis, 18 Ind. App. 525, 48 N. E. Rep. 646.

[8] False imprisonment by act of agent, see Central, etc., R. Co. v. Brewer

corporation and can act only through agents. The negligence of the superintending agent should be considered the negligence of the corporation, and when exemplary damages could have been recovered against such an agent, it should be allowed against the corporation.[1] A corporation should be held liable for punitive damages when an individual would be liable under the same circumstances.[2] The decisions, however, are conflicting and may be divided into three classes.

(1) Those holding that only actual damages can be recovered.[3]

(2) Those allowing punitive damages when the wrongful act of the agent or employe was willful and intentional.[4]

(3) Those allowing punitive damages only when the wrongful act was done under the express direction of the corporation or afterwards ratified by the corporation.[5]

§ 236. **The commission of crime.**—There are some crimes which a corporation, from its nature, can not commit, but generally it is subject to indictment and punishment by fine like a natural person. The capacity of a corporation to com-

78 Md. 394, 27 L. R. A. 63; Gillingham v. Ohio, etc., R. Co., 35 W. Va. 588, 14 L. R. A. 798; Palmeri v. Manhattan R. Co., 133 N. Y. 261, 16 L. R. A. 136, and note to Mulligan v. New York, etc., R. Co., 14 L. R. A. 791. Conspiracy, Buffalo, etc., Co. v. Standard, etc., Co., 106 N. Y. 669.

[1] Shearman & Redfield Neg., II, § 749; Denver, etc., R. Co. v. Harris, 122 U. S. 597; Alabama, etc., R. Co. v. Sellers, 93 Ala. 9, 30 Am. St. Rep. 17.

[2] Denver, etc., R. Co. v. Harris, 122 U. S. 597; Wheeler & Wilson, etc., Co. v. Boyce, 36 Kan. 350; Western, etc., Co. v. Eyser, 2 Colo. 141; New Orleans, etc., R. Co. v. Bailey, 40 Miss. 395; Atlantic, etc., R. Co. v. Dunn, 19 Ohio St. 162.

[3] Wardrobe v. California, etc., Co., 7 Cal. 119; Turner v. North Beach, etc., R. Co., 34 Cal. 594; Mendelsohn v. Anaheim, etc., Co., 40 Cal. 657; Hays v. Houston, etc., R. Co., 46 Tex. 272; Ackerson v. Erie R. Co., 32 N. J. L. 254; Detroit, etc., Co. v. McArthur, 16 Mich. 447.

[4] Denver, etc., R. Co. v. Harris, 122 U. S. 597; Milwaukee, etc., R. Co. v. Arms, 91 U. S. 489; Philadelphia, etc., R. Co. v. Quigley, 21 How. 202; New Orleans, etc., R. Co. v. Burke, 53 Miss. 200; Baltimore, etc., R. Co. v. Boone, 45 Md. 344; Samuels v. Evening Mail, 75 N. Y. 604; Jeffersonville, etc., R. Co. v. Rogers, 38 Ind. 116; Goddard v. Grand Trunk R. Co., 57 Me. 202; Taylor v. Grand Trunk R. Co., 48 N. H. 304; Belknap v. Boston, etc., R. Co., 49 N. H. 358.

[5] Beers v. Hamburg-American, etc., Co., 62 Fed. Rep. 469; Hagan v. Providence, etc., R. Co., 3 R. I. 88; Nash-

mit a crime is thus stated by Bishop:[1] "A corporation can not, in its corporate capacity, commit a crime by an act in the fullest sense *ultra vires* and contrary to its nature. But within the sphere of its corporate capacity, and to an undefined extent beyond,[2] whenever it assumes to act as a corporation it has the same capabilities of criminal intent and of act—in other words, of crime—as an individual man sustaining to the thing the like relation."

A corporation was indictable at common law,[3] but the subject is now largely regulated by statute.[4] The better rule is that a corporation is a "person" within the meaning of criminal statutes,[5] although the cases are not uniform.[6]

In the early cases a distinction was made between acts of nonfeasance and acts of misfeasance, and it was held that a corporation could be punished criminally for acts of nonfeasance only.[7] But this distinction is now discarded, at least where no criminal intent is involved.[8] A corporation is liable for keeping a disorderly house,[9] obstructing a highway,[10] maintaining a nuisance, publishing a libel, as well as for failing to

ville, etc., R. Co. v. Starnes, 9 Heisk. 52; Bass v. Chicago, etc., R. Co., 42 Wis. 654; Malecek v. Tower Grove, etc., R. Co., 57 Mo. 17; Travers v. Kansas Pac R. Co., 63 Mo. 421; Galveston, etc., R. Co. v. Donahoe, 56 Tex. 162; Emerson, etc., Co. v. Skidmore (Tex., 1894), 25 S. W. Rep. 671.

[1] Bishop New Criminal Law, § 417; McClain Criminal Law, § 180.

[2] Bishop Non-Contract Law, § 719.

[3] Reg. v. Birmingham, etc., R. Co., 9 C. & P. 469; State v. Security Bank, 2 S. Dak. 538; Commonwealth v. Lehigh, etc., R. Co., 165 Pa. St. 162; Commonwealth v. Pulaski, etc., Assn., 92 Ky. 197, 17 S. W. Rep. 442; State v. The Morris, etc., R. Co., 23 N. J. L. 360; State v. Baltimore, etc., R. Co., 15 W. Va. 362, citing many cases.

[4] See State v. Western, etc., R. Co., 89 N. C. 584.

[5] McClain Criminal Law, § 181; State v. Baltimore, etc., R. Co., 15 W. Va. 362.

[6] State v. Cincinnati, etc., Co, 24 Ohio St. 611; State v. Field, 49 Mo. 270.

[7] State v. Great Works, etc., Co., 20 Me. 41; State v. Baltimore, etc., R. Co., 120 Ind. 298.

[8] Pittsburgh, etc., R. Co. v. Commonwealth, 101 Pa. St. 192; State v. Vermont, etc., R. Co., 27 Vt. 103; State v. The Morris, etc., R Co., 23 N. J. L. 360; State v. Railway Co., 15 W. Va. 362; Commonwealth v. Pulaski, etc., Assn., 92 Ky. 197.

[9] State v. Passaic, etc., Soc., 54 N. J. L. 260.

[10] Reg. v. Great North, etc., R. Co., 2 Cox Cr. Cas. 70; Northern, etc., R. Co. v. Commonwealth, 90 Pa. St. 300; State v. Chicago, etc., R. Co., 77 Iowa 442.

construct a bridge or do some other act imposed by law.[1] In a prosecution of an agricultural fair association for permitting gaming upon its grounds the court said:[2]

"It is, therefore, now well settled in the courts of this country, as well as in England, that they are indictable for misfeasance as well as a nonfeasance of duty unlawful in itself and injurious to the public. It has, therefore, been held that they may be indicted for a nuisance, whether arising from misfeasance or nonfeasance, or for an injury otherwise to the public unlawful in itself, and arising either from commission or the omission to perform a legal duty. They may be indicted for erecting and continuing a building, for leaving railroad cars in a street; for neglecting to repair a highway; for permitting stagnant water to remain on their premises; for libel; for "Sabbath breaking," by doing work on Sunday in violation of the statute, and in many other instances. It is true there are crimes of which, from their very nature, as perjury, for example, they can not be guilty. There are crimes to the punishment for which, for a like reason, they can not be subjected, as in the case of a felony. But wherever the offense consists in either a misfeasance or a nonfeasance of duty to the public, and the corporation can be reached for punishment, as by a fine and the seizure of its property, precedent authorizes, and public policy requires, that it should be liable to indictment. Any other rule would in many cases preclude adequate remedy, and leave irresponsible servants, rather than those who are really most at fault. If it be said that such a rule may subject the property of innocent stockholders for the acts of the directors, to which they are not actual parties and of which they had no knowledge, the answer is that they select directors, and it is their business to have those who will see that the corporate business is so con-

[1] Commonwealth v. Pennsylvania, R. Co., 117 Pa. St. 637; State v. Madison, 63 Me. 546, New York, etc., R. Co. v. State, 50 N. J. L. 303, 53 N. J. L. 244.

[2] Commonwealth v. Pulaski, etc., Assn., 92 Ky. 197. See an extensive review of the early cases in State v. The Morris, etc., R. Co., 23 N. J. L. 360.

ducted as not to injure others or infringe upon public right and good order in the community. If the penalty prescribed for the act be both fine and imprisonment, then, so far as the punishment can not, from the nature of the offender, be carried out, the statute is, of course, inoperative."

§ 237. **Crimes involving intent.**—The crimes referred to in the preceding section, which from their nature corporations can not be guilty of, are those which involve criminal intent and include practically all the common law felonies, such as murder, assault and battery and larceny. Such crimes are the crimes of the individual officers or agents of the corporation.[1] Thus, acts which make it criminal to "knowingly and willfully" do an act, such as employing children in a factory who are under a certain age, do not apply to corporations.[2]

By the modern doctrine a corporation is liable civilly for punitive damages caused by an assault and battery[3] or a malicious prosecution and other torts involving intent, and there is a tendency toward extending this rule so as to include criminal liability for such offenses.[4]

"Corporations can not be indicted for offenses which derive their criminality from evil intention, or which consist in a violation of those social duties which appertain to men and subjects. They can not be guilty of treason or felony, or perjury or offenses against the person. But beyond this there is no good reason for their exemption from the consequences of unlawful and wrongful acts committed by their agents in pursuance of authority derived from them."[5]

§ 238. **Contempt of court.**—A corporation may be guilty of a contempt of court, and may be punished therefor by a fine, as in

[1] Cumberland, etc., Co. v. Portland, 56 Me. 77.

[2] Menson v. Manufacturing Co., 9 Met. (Mass.) 562; Androscoggin, etc., Co. v. Bethel, etc., Co., 64 Me. 441.

[3] Eastern, etc., R. Co. v. Broom, 6 Exch. 314; Denver, etc., R. Co. v. Harris, 122 U. S. 597; McKinley v. Chicago, etc., R. Co., 44 Iowa 314, 24 Am. Rep. 748.

[4] See State v. Passaic Co. Agr. Soc., 54 N. J. L. 260.

[5] Commonwealth v. Prop. New Bedford Bridge, 2 Gray (Mass.) 339.

the case of a natural person.[1] Contempt proceedings are criminal,[2] but the defendant has no right to a jury trial.[3]

§ 239. **Proceedings.**—The difficulties arising on the application of the rule that corporations may be prosecuted for the commission of crimes are principally those of procedure. In some states the statutes provide in detail for the proceedings. The proceeding is illustrated by the Minnesota statute which provides that when a corporation is indicted a summons signed by one of the judges of the court into which the indictment is returned shall be issued by the clerk, commanding the sheriff to forthwith notify the accused and command its appearance before the court within twenty-four hours from the time of such service. Summons may be served in the manner provided for the service of process in a civil action. The corporation is required to appear within the time mentioned in the summons by one of its officers or by counsel; and the proceedings thereafter are the same as in ordinary cases upon similar charges. If the corporation fails to appear within the time stated, a plea of not guilty is entered by the clerk, and thereafter the corporation is deemed continually present in court till the final determination of the action. If found guilty, a fine is imposed which is docketed as a judgment against the corporation, and is enforced like a judgment in a civil action.[4]

[1] Golden Gate, etc., Min. Co. v. Superior Court, 65 Cal. 187; Mayor, etc., of New York v. New York, etc., Co., 64 N. Y. 622; United States v. Memphis, etc., R. Co., 6 Fed. Rep. 237; Telegram, etc., Co. v. Comm., 52 N. E. Rep. 445 (Mass., 1899), Wilgus' Cases.

[2] Smith v. Whitfield & Sanders, 38 Fla. 211.

[3] People v. Kipley, 171 Ill. 44.

[4] Gen. Laws Minn., 1895, chap. 217.

CHAPTER 11.

EXTRA-TERRITORIAL POWERS OF CORPORATIONS—STATE CONTROL OVER FOREIGN CORPORATIONS.

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§ 240. **General statement.**—The subject-matter of this chapter falls within the domain of private international law and is of great importance by reason of the intimate commercial relations of the states of the Union. The rights and privileges of corporations beyond the jurisdiction of the sovereignty by which they are created are governed in part by the rules of comity and in part by express statutes. For certain purposes corporations are recognized as persons, but they are not citizens of a state within the meaning of the provision of the constitution of the United States which secures to the citizens of each state all the privileges of citizens of the several states.[1] These artificial persons are accorded recognition in foreign states when their organization and object is not in conflict with the policy of the foreign state. "The natural persons belonging to the state," says Bar,[2] "are recognized as persons in every other state. This undoubted rule is a consequence of the equality of natives and foreigners admitted by modern international law. But by custom it is just as fully recognized that legal persons belonging to another state must also be so regarded. * * * Although the authority of the foreign state by which legal personalities are either directly created, or their creation by private persons tolerated, has no weight in one state for itself, yet modern international intercourse requires the same recognition to be extended even to the legal personalities which may be capriciously created. * * * If the state in which it is proposed to establish the undertaking will not permit it to be established, the object of the association * * * can never be attained. A foreign state which should recognize as a legal person what was not so recognized in its own state, would be treating as valid legal facts directed to ends that are either legally or actually impossible—a result at variance with general logical principles."

§ 241. **The corporate domicile.**—A corporation has its domicile in the state by which it was created,[3] but by acquiring a

[1] § 65, *supra*.
[2] Priv. Int. Law, § 41.
[3] Wharton's Conf. of Laws, § 489; Story's Conf. of Laws, § 38; Merrill, Comp. Jur., 80; Westlake Priv. Int. Law, p. 259; Calcutta Jute Co.

place of business in another state it may for certain purposes acquire a domicile there also.[1]

§ 242. **Laws have no extra-territorial force.**—The laws of a state have no force or effect, *ex propria vigore*, beyond the territorial limits of the state. "It is the indubitable basis of universal law," says Story, that "laws have no force beyond the territories of those who make them. This is one of the few principles of universal jurisprudence universally acknowledged."[2]

The same learned writer says: "The power of a corporation to act in a foreign country depends both upon the law of the country where it was created and on the law of the country where it assumes to act. It has only such powers as were given it by the authority which created it. It can not do any act by virtue of those powers in any country where the law forbids it so to act. It follows that every country may impose conditions and restrictions upon foreign corporations which transact business within its limits."[3] Although laws have no extra-territorial force the general rule is that things done in one state in pursuance of the laws thereof are valid and binding in other states.[4]

§ 243. **Submission to state laws.**—A corporation by engaging in business in a foreign state submits itself to the jurisdic-

v. Nicholson, L. R. 1 Ex. Div. 428.

[1] Smith v. Pilot, etc., Co., 47 Mo. App. 409; Young v. South Tredegar I. Co., 85 Tenn. 189; 4 Am. St. Rep. 752.

[2] Story's Conf. of Laws, §§ 29, 38, 278; Westlake Priv. Int. Law, § 132; Rorer Inter-state Law, p. 167; Pennoyer v. Neff, 95 U. S. 714. It is an ancient maxim that "beyond his territorial boundaries it is not safe to obey a party commanding. United States v. Bevans, 3 Wheat. 336, 3 Dall. 370 note; Henry's Foreign Law, § 1. The only force allowed to laws extra-territorially is derived from international comity, which never intervenes to set aside either the written law or the common law, or even the state policy or state interest of another country. Bank of Augusta v. Earle, 13 Pet. 517.

[3] Conflict of Laws, § 106, *note a*.

[4] American, etc., Co. v. Farmers', etc., Co., 20 Colo. 203, 25 L. R. A. 338. A statute providing that an association or partnership can be sued in its company name has no extra-territorial force. Edwards v. Warren, etc., Works, 168 Mass. 564, 38 L. R. A. 791, Wilgus' Cases.

tion and becomes subject to the laws of such state. Thus, such a corporation becomes subject to the law of the foreign state which prohibits garnishment or other proceedings to defeat the exemption of the wages of a debtor on a contract to be performed in that state.[1] So, a foreign insurance corporation which avails itself of the privilege of doing business under the restrictions of a statute is not permitted to assert that the statute is unconstitutional.[2]

§ 244. **Conflict of laws.**—As already stated, a corporation submits itself to the laws of a state by qualifying and engaging in business in such state. Its contracts, however, receive their sanction from the law of the place where they are executed and to be performed, and their interpretation is controlled by the *lex loci*.[3] The place of making a contract is presumed to be the place of its performance in the absence of anything indicating a contrary intention.[4] An express provision in a contract that it shall be construed in a certain state, makes it a contract of that state.[5] Assignments of personal property, valid by the law of the domicile, are generally recognized as valid by the law of the state where the property is situated, unless in violation of the law or public policy of that state.[6] The legality of a bequest to a foreign corporation is generally governed by the laws of the forum, although it may differ from the law of the state by which the corporation was

[1] Singer, etc., Co. v. Fleming, 39 Neb. 679, 23 L. R. A. 210.

[2] Daggs v. Orient, etc., Co., 136 Mo. 382, 35 L. R. A. 227.

[3] Heaton v. Eldridge & Higgins, 56 Ohio St. 87, 36 L. R. A. 817; Crumlish's Adm'rs v. Central, etc., Co., 38 W. Va. 390, 23 L. R. A. 120. Executing a reinstatement in one state of an insurance policy made in another does not destroy the character of the policy as a contract of the state where it was originally issued. Goodwin v. Providence, etc., Assn., 97 Iowa 226.

[4] Tillinghast v. Boston, etc., Co., 39 S. C. 484, 22 L. R. A. 49.

[5] Union, etc., Co. v. Pollard, 94 Va. 146, 36 L. R. A. 271.

[6] Vanderpool v. Gorman, 140 N. Y. 563, 24 L. R. A. 548. But see Barth v. Backus, 140 N. Y. 230, 23 L. R. A. 47. A foreign corporation may make an assignment of property in New York if it could have done so in the state of its domicile. Rogers v. Pell, 154 N. Y. 518.

created.[1] The liability of stockholders in foreign corporations is determined by the law of the creating state,[2] but there is great difficulty in its enforcement. It is sometimes said that it can only be enforced at the domicile of the corporation,[3] but the weight of authority is otherwise.[4] In all cases the procedure of the forum must govern, and if no procedure or an inconsistent procedure is provided by the law of the forum, the liability can not be enforced.[5] Where the liability is penal and not contractual, it can not be enforced outside the state.[6] The local laws governs a policy of insurance on real property delivered to the owner in the state where the property is situated.[7] When there is a failure to show the law of another state which governs the rights of a foreign corporation the case will be governed by the law of the forum.[8]

§ 245. **Obligations imposed by penal statutes.**—Causes of action which arise out of penal statutes can not be prosecuted in a foreign state.

In a case which arose under a statute which made directors personally liable to creditors for making and signing a false report, the supreme court of the United States said:[9]

[1] Congregational, etc., Soc. v. Everett, 85 Md. 79, 35 L. R. A. 693.

[2] Mandel v. Swan, etc., Co., 154 Ill. 177, 27 L. R. A. 313.

[3] Marshall v. Sherman, 148 N. Y. 9, 34 L. R. A. 757.

[4] Hale v. Hardin, 95 Fed. 947.

[5] Rhodes v. U. S. Nat. Bank, 24 U. S. App. 607, 66 Fed. Rep. 512, 34 L. R. A. 742; Ferguson v. Sherman, 116 Cal. 169, 37 L. R. A. 622. See 42 L. R. A. 396, and cases cited.

[6] Tuttle v. National Bank of the Republic, 161 Ill. 497, 34 L. R. A. 750; Russell v. Pacific R. Co., 113 Cal. 258, 34 L. R. A. 747. See Marshall v. Sherman, 148 N. Y. 9.

[7] Daggs v. Orient, etc., Co., 136 Mo. 382, 35 L. R. A. 227. In Mullen v. Reed, 64 Conn. 240, 24 L. R. A. 664, it was held that the words "heirs at law" in a policy made in Massachusetts, must be given the meaning it would have in Massachusetts.

[8] Bath, etc., Co. v. Claffy, 151 N. Y. 24, 36 L. R. A. 664.

[9] Huntington v. Attrill, 146 U. S. 657. Mr. Justice Gray said: "It is true that the courts of some states, including Maryland, have declined to enforce a similar liability imposed by the statute of another state. But in each of these cases it appears to have been assumed to be a sufficient ground for that conclusion that the liability was not founded in contract, but was in the nature of a penalty imposed by statute, and no reasons were given for considering the statute a penal law in the strict, primary and international sense. Derrickson v

"The provision of the statute of New York, now in question, making the officers of a corporation who sign and record a false certificate of the amount of its capital stock liable for all its debts, is in no sense a criminal or *quasi*-criminal law. The statute, while it enables persons complying with its provisions to do business as a corporation, without being subject to the liability of general partners, takes pains to secure and maintain a proper corporate fund for the payment of the corporate debts. With this aim it makes the stockholders individually liable for the debts of the corporation until the capital stock is paid in and a certificate of the payment made by the officers, and makes the officers liable for any false and material representation in that certificate. The individual liability of the stockholders takes the place of a corporate fund until that fund has been duly created, and the individual liability of the officers takes the place of the fund in case their statement that it has been duly created is false. If the officers do not truly state

Smith, 3 Dutcher (27 N. J. L.) 166; Halsey v. McLean, 12 Allen 438; First National Bank v. Price, 33 Md. 487. It is also true that in Steam, etc., Co. v. Hubbard, 101 U. S. 188, 192, Mr. Justice Clifford referred to those cases by way of argument. But in that case, as well as in Chase v. Curtis, 113 U. S. 452, the only point adjudged was that such statutes were so far penal that they must be construed strictly, and in both cases jurisdiction was assumed by the circuit court of the United States, and not doubted by this court, which could hardly have been if the statute had been deemed penal within the maxim of international law. In Flash v. Connecticut, 109 U. S. 371, the liability sought to be enforced under the statute of New York was the liability of a stockholder arising upon contract, and no question was presented as to the nature of the liability of officers. But in Hornor v. Henning, 93 U. S. 228, this court declined to consider a similar liability of officers of a corporation in the District of Columbia as a penalty. See also Neal v. Moultrie, 12 Ga. 104; Cady v. Sanford, 53 Vt. 632, 639, 640; Nickerson v. Wheeler, 118 Mass. 295, 298; Post v. Toledo, etc., R. Co., 144 Mass. 341, 345; Wolverton v. Taylor, 132 Ill. 197; Morawetz on Corporations (2d ed.), § 908. * * * In this view that the question is not one of local but of international law, we fully concur. The test is not by what name the statute is called by the legislature or the courts of the states in which it is passed, but whether it appears to the tribunal which is called upon to enforce it to be, in its essential character and effect, a punishment of an offense against the public, or a grant of a civil right to a private person." As to penalty for failure to send a telegraph message, see Carnahan v. Western, etc., Co., 89 Ind. 526.

and record the facts which exempt them from liability they are made liable directly to every creditor of the company who by reason of their wrongful acts has not the security for the payment of his debt out of the corporate property, on which he had a right to rely. As the statute imposes a burdensome liability on the officers for their wrongful act, it may well be considered penal, in the sense that it should be strictly construed. But as it gives a civil remedy at the private suit of the creditor only, and measured by the amount of his debt it is as to him clearly remedial. To maintain such a suit is not to administer a punishment imposed upon an offender against the state, but simply to enforce a private right secured under its laws to an individual. We can see no just ground, on principle, for holding such statute to be a penal law, in the sense that it can not be enforced in a foreign state or country."

§ 246. **Constitutional rights of corporations—Insolvency proceedings.**—A corporation is a person within the meaning of the first section of the fourteenth amendment to the constitution of the United States, and may, therefore, invoke the benefit of those provisions of the constitution which guarantee to persons the enjoyment of property or afford them the means for its protection or prohibit legislation injuriously affecting it.[1] Neither the provision that the citizens of one state shall be entitled to all the privileges and immunities of citizens of the several states, nor, that no state shall deny to any person within its jurisdiction the equal protection of its laws, requires a state to recognize the corporation of another state.[2] A discharge under a state insolvent law does not bar the claim of a

[1] Louisville, etc., Co. v. Louisville, etc., Co., 92 Ky. 233, 14 L. R. A. 579, annotated; Santa Clara County v. Southern, etc., R. Co., 118 U. S. 394, 396, 30 L. ed. 118; Pembina, etc., Co. v. Pennsylvania, 125 U. S. 181, 31 L. ed. 650, 2 Inters. Com. Rep. 24; Minneapolis, etc., R. Co. v. Beckwith, 129 U. S. 26, 28, 32 L. ed. 585, 586; Hammond, etc., Co. v. Best, 91 Me. 431, 42 L. R. A. 528. See also United States v. Northwestern, etc., Co., 164 U. S. 686, 41 L. ed. 599. § 68, *supra*. As to constitutional rights of corporations, see People v. Fire Assn., etc., 92 N. Y. 311.

[2] Pembina, etc., Co. v. Pennsylvania, 125 U. S. 181; Norfolk, etc., Co. v. Pennsylvania, 136 U. S. 114.

creditor who does not voluntarily submit to the jurisdiction of the insolvency court, where the creditor is a citizen of another state, a corporation beyond the jurisdiction of the court, or a resident of a foreign country and beyond the jurisdiction of the court.[1] Hence, a foreign corporation is not bound by the discharge of its debtor in state insolvency proceedings, when it has not proved its claim or accepted a dividend thereon, although it has an established place of business in the state at which statutory service upon it is made in such proceedings.[2] The court said: "The defendant concedes that if the plaintiff were a natural person instead of a corporation, and in the same condition that the corporation is, his discharge in insolvency could not be successfully pleaded in discharge of the debt.[3] But it is contended that the same rule that would be applied to an individual creditor living in a state other than our own should not apply where the creditor is a foreign corporation occupying a store and doing business in this state. We do not see that in principle there is any force in such a distinction. Creditors without any corporate authority, who have their residence out of the state, may hire and occupy stores and sell merchandise within the state, and their debts contracted here not be affected by their debtor's insolvency, and why may not a foreign corporation just as well have the same immunity?" A foreign corporation which has complied with the statute and is doing business in the state is not a resident of the state within the meaning of the statute,[4] and is not precluded from recovering for goods sold to a resident, by a discharge of the debtor in insolvency proceedings.[5] A foreign corporation which does not do business in a state is not within the jurisdiction and is not entitled to the protection of its laws.

[1] Baldwin v. Hale, 1 Wall. 223; Gilman v. Lockwood, 4 Wall. 409; Denny v. Bennett, 128 U. S. 489; Felch v. Bugbee, 48 Me. 9, 77 Am. Dec. 203; Hills v. Carlton, 74 Me. 156; Pullen v. Hillman, 84 Me 129; Silverman v. Lessor, 88 Me. 599; Phœnix, etc., Bank v. Batcheller, 151 Mass. 589, 8 L. R. A. 644.

[2] Hammond, etc., Co. v. Best, 91 Me. 431, 42 L. R. A. 528, Wilgus' Cases.

[3] Pullen v. Hillman, 84 Me. 129.

[4] Mass. Pub. Stat. 1895, ch. 157, § 81.

[5] Bergner, etc., Co. v. Dreyfus (Mass., 1899), 51 N. E. Rep. 531.

The state may, therefore, discriminate against it in the distribution of the assets of another corporation.[1]

I. Right of a Corporation to Exercise its Powers in a Foreign State.

§ 247. **Power of corporation.**—It follows from the doctrine above stated that a state can not empower a corporation to exercise its powers and franchises in another state without the consent of the foreign state. It has been said that a corporation must "dwell in the place of its creation and can not migrate to another sovereignty."[2] This is true only in the sense that it can not act *as a corporation* beyond the jurisdiction of its creation, but *it may transact such business and do such acts in the foreign jurisdiction as a natural person might do.* Thus a corporation can not hold corporate meetings in a foreign jurisdiction, but it may, through its agents, transact business there when not forbidden to do so by the laws of the foreign state.[3] Hence, a corporation may make valid contracts in a foreign state subject to the restrictive laws of that state,[4]

[1] Blake v. McClung, 172 U. S. 239. See § 65, *supra*. Two justices dissenting. In Fritts v. Palmer, 132 U. S. 282, a Colorado statute which provided that a mortgage given by a foreign corporation on property in the state for a debt created in another state should not take effect as against persons in that state until the liabilities due to them at the time when the mortgage was recorded was paid, was held constitutional. As to the power of the state to discriminate against non-resident creditors in the matter of attachments upon the property of insolvents, see Long v. Girdwood, 150 Pa. St. 413, 23 L. R. A. 33.

[2] See comment upon this language in Shaw v. Quincy, etc., Co., 145 U. S. 444, Wilgus' Cases.

[3] Murfree For. Corps., § 14; Wharton Conf. of Laws, § 105*a*; Westlake, Priv. Int. Law, § 288; Franco-Texan, etc., Co. v. Laigle, 59 Tex. 339; Ormsby v. Vermont, etc., Co., 56 N. Y. 623. See the criticism on the dictum of Chief Justice Taney that a corporation can not migrate to another sovereignty, in Bigelow's note to Story's Conf. of Law, p. 178.

[4] Merrick v. Van Santvoord, 34 N. Y. 208; Day v. Ogdensburg, etc., R. Co., 107 N. Y. 129; Newburg, etc., Co. v. Weare, 27 Ohio St. 343; Atchison, etc., R. Co. v. Fletcher, 35 Kan. 236. In Canada, etc., R. Co. v. Gebhard, 109 U. S. 527, Chief Justice Waite said: "A corporation 'must dwell in the place of its creation, and can not migrate to another sovereignty,' though it may do business in all places where its charter allows and the local laws do not forbid." Railroad Co. v. Koontz, 104 U. S. 5. But wher-

and governed by the laws of the state which created the corporation.[1] A corporation is clothed everywhere with the character given by its charter, and the capacity of corporations to make contracts beyond the states of their creation, and the exercise of that capacity, are supported by uniform, universal and long-continued practice.[2] In discussing the limitations upon the extra-territorial acts of a foreign corporation, Mr. Murfree says:[3] "The recognition which is by comity extended to foreign corporations does not vest them with an unrestricted faculty of extra-territorial action, even within the limits of their charter powers; while the cases are not uniform on this point, yet the weight of authority seems to be that the company's power in the foreign jurisdiction extends only to those acts which may be done through the mediation of agents. Those corporate acts which must be done by the company itself, through the persons of the corporators or stockholders, must be performed where the company has a legal existence. The most obvious of these are meetings for the acceptance of the charter and organization of the corporation." Hence, a legal meeting of the board of directors, who are merely agents, may be held beyond the borders of the state.[4] In order to comply with the requirement of a foreign state, a corporation has power to deposit securities with an official of the foreign state.[5]

ever it goes for business it carries its charter, as that is the law of its existence, and the charter is the same abroad that it is at home. Whatever disabilities are placed upon the corporation at home it retains abroad, and whatever legislative control it is subjected to at home must be recognized and submitted to by those who deal with it elsewhere."

[1] Manhattan, etc., Co. v. Fields (Tex., 1894), 26 S. W. Rep. 280; Rue v. Railway Co., 74 Tex. 474. See Falls v. U. S., etc., Assn., 97 Ala. 417, 24 L. R. A. 174, decision on rehearing.

[2] Land Grant R. Co. v. Coffey Co., 6 Kan. 245; O'Brien v. Wetherell, 14 Kan. 616; Cowell v. Springs Co., 100 U. S. 55.

[3] Murfree For. Corp., § 8.

[4] Galveston, etc., R. Co. v. Cowdrey, 11 Wall. (U. S.) 459; Arms v. Conant, 36 Vt. 743; Wright v. Bundy, 11 Ind. 398; Reichwald v. Commercial Hotel, 106 Ill. 439; Bellows v. Todd, 39 Iowa 209; Missouri, etc., Co. v. Reinhard, 114 Mo. 218.

[5] Lewis v. American, etc., Assn., 98 Wis. 203, 39 L. R. A. 559.

§ 248. **Corporate acts out of state.**—A corporation has no power, in the absence of express authority, to perform strictly corporate acts outside of the state of its creation.[1] No legal organization of a corporation can take place at a meeting held outside of the state granting the charter.[2] But where all the interested parties acquiesce, corporate acts done beyond the limits of the state may be binding.[3] Authority to transact business at places out of the state does not authorize corporate acts, such as corporate meetings.[4] In a leading case in Maine[5] the question was on the validity of a certain mortgage executed by the officers of a corporation, elected at a meeting held out of the state for the organization of the corporation. The corporation was created by the state of Vermont. It appeared from the records of the corporation that a meeting of the corporators was called for the organization of the corporation under its charter, in the city of New York, and that the charter was there accepted, and the officers of the corporation elected. Chief Justice Shepley said: "There are a variety of corporations. It will only be necessary on this occasion to speak of one class of them—corporations aggregate composed of natural persons. It is often stated in the books that such a corporation is created by its charter. This is not precisely correct. The charter only confers the power of life, or the right to come into existence, and provides the instruments by which it may become an artificial or acting entity. Such a corporation has been well defined to be an artificial being, invisible, intangible, and existing only in contemplation of law. The instruments provided to bring the artificial being into life and active operation are the persons named in the charter, and those who, by virtue of its provisions, may become associated

[1] Bastian v. Modern Woodmen of America, 166 Ill. 595.

[2] Freeman v. Machias, etc., Co., 38 Me. 343; Ormsby v. Vermont, etc., Co., 56 N. Y. 623; Mitchell v. Vermont, etc., Co., 67 N. Y. 280; Smith v. Silver Valley, etc., Co., 61 Md. 85; Camp v. Byrne, 41 Mo. 525; Hodgson v. Duluth, etc., R. Co., 46 Minn. 454, under statute.

[3] Missouri, etc., Co. v. Reinhard, 114 Mo. 218, Wilgus' Cases.

[4] Franco-Texan, etc., Co. v. Laigle, 59 Tex. 339. See Hodgson v. Duluth, etc., R. Co., 46 Minn. 454.

[5] Miller v. Ewer, 27 Me. 509, 46 Am. Dec. 619, Wilgus' Cases.

with them. Those persons or corporations, as natural persons, have no such power. The charter confers upon them a new faculty for this purpose; a faculty which they can have only by virtue of the law which confers it. That law is inoperative beyond the bounds of the legislative power by which it is enacted. As the corporate faculty can not accompany the natural persons beyond the bounds of the sovereignty which confers it, they can not possess or exercise it there; can have no more power there to make the artificial being act, than other persons not named or associated as corporators. Any attempt to exercise such a faculty there is merely an usurpation of authority by persons destitute of it, and acting without any legal capacity to act in that manner. It follows that all votes and proceedings of persons professing to act in the capacity of corporators, when assembled without the bounds of the sovereignty granting the charter, are wholly void. * * * It may maintain a suit without those limits, but that does not imply its existence or presence there. It may also contract without those limits. Being within them, it may, acting *per se*, by vote transmitted elsewhere, propose a contract or accept one previously offered. And it may, by an agent or agents duly constituted, act and contract beyond those limits. But it can neither exist nor act *per se* without them, except by the existence of its officers or agents, duly elected or appointed within them."[1]

II. Power of the State Over Foreign Corporations.

§ 249. **Right to exclude.**—For the purposes of jurisdiction the states of the Union are foreign to each other;[2] and as corporations are the mere creatures of legislation, it follows that a state may exclude a foreign corporation from doing business within its limits, or may grant such corporation a license to do business upon such terms and conditions as the peculiar in-

[1] As to the distinction between corporate and other acts, see also Freeman v. Machias, etc., Co., 38 Me. 343; Ormsby v. Vermont, etc., Co., 56 N. Y. 623; Jones v. Pearl, etc., Co., 20 Colo. 417.

[2] See Williams v. Kimball, 35 Fla. 49, 26 L. R. A. 746.

terests and policy of the state may require.[1] "Every power which a corporation exercises in another state depends for its validity upon the laws of the sovereignty in which it is exercised, and a corporation can make no valid contract without the sanction, express or implied, of such sovereignty; unless a case should be presented in which the right claimed by the corporation should appear to be secured by the constitution of the United States."[2] The recognition of its existence "depends purely upon the comity of other states—a comity which is never extended where the existence of the corporation or the exercise of its powers is prejudicial to their interests or repugnant to their policy. Having no absolute right of recognition in other states, but depending for such recognition or the enforcement of its contracts upon their assent, it follows as a matter of course that such assent may be granted upon such terms and conditions as those states may think proper to impose. They may exclude the foreign corporation entirely; they may restrict its business to particular localities, or they may exact such security for the performance of its contracts with their citizens as in their judgment will best promote the public interests. The whole matter rests in their discretion."[3] There are many good and sufficient reasons why a state should choose to modify the rule of comity, and impose restrictions upon a foreign corporation. As said by Mr. Justice Field, "it is not every corporation, lawful in the state of its creation, that other states may be willing to admit within their jurisdiction, or consent that it have officers in them; such, for example, as a corporation for lotteries. And even when the business of a foreign corporation is not unlawful in other states, the latter may wish to limit the number of such corporations,

[1] Wharton's Conf. of Laws, § 104*a*; Greene's Brices *Ultra Vires*, p. 4, note a; Paul v. Virginia, 8 Wall. (U. S.) 168; Commonwealth v. New York, etc., R. Co., 129 Pa. St. 463; Phœnix, etc., Co. v. Burdett, 112 Ind. 204; Phœnix, etc., Co. v. Welch, 29 Kan. 672; Hartford, etc., Co. v. Raymond, 70 Mich. 485; State v. Phœnix, etc., Co., 92 Tenn. 420.

[2] Runyan v. Coster's Lessees, 14 Pet. (U. S.) 122–129.

[3] Paul v. Virginia, 8 Wall. (U. S.) 168; Wyman v. Kimberly-Clark Co., 93 Wis. 554.

or subject their business to such control as would be in accordance with the policy governing domestic corporations of a similar character.'"[1]

In Florida it is held that a corporation organized under the laws of another state must also become incorporated under its laws, and a failure to do so makes the members liable as partners.[2] A state can not by mere legislative enactment make all foreign corporations domestic corporations of that state, and thus deprive them of the right to resort to the federal courts.[3]

§ 250. **Limitations on the power of the state.**—The general rule stated in a preceding section that a state may entirely exclude foreign corporations from doing business within its limits, or permit them to do business upon complying with prescribed conditions, is, however, subject to the limitations imposed by the federal constitution, which grants to congress exclusive control over interstate commerce. Hence, a state can not exclude or regulate the business of a foreign corporation, which is engaged in interstate commerce, or which is itself an agency of the national government.[4]

A contract between a resident of the state and a foreign cor-

[1] Pembina Mining Co. v. Pennsylvania, 125 U. S. 181; Paul v. Virginia, 8 Wall. 168; Runyan v. Coster, 14 Pet. 122; Canada Southern Ry. Co. v. Gebhard, 109 U. S. 527; Demarest v. Flack, 128 N. Y. 205; Isle, etc., Corporation v. Osmun, 76 Mich. 162. A foreign corporation can exercise its franchises in Pennsylvania only so far as it may be permitted by the local sovereign. The right rests wholly in the comity of states. A corporation of one state can not do business in another state without the latter's consent, express or implied, and that consent may be accompanied with such conditions as the latter may think proper to impose. These conditions will be valid and effectual, provided they are not repugnant to the constitution or laws of the United States, etc. Commonwealth v. New York, etc., R. Co., 129 Pa. St. 463; St. Clair v. Cox, 106 U. S. 350.

[2] Taylor v. Branham, 35 Fla. 297, 39 L. R. A. 362.

[3] Rece v. Newport News, etc., R. Co., 32 W. Va. 164, 3 L. R. A. 572.

[4] Crutcher v. Kentucky, 141 U. S. 47; Pensacola, etc., Co., v. Western U. Tel. Co., 96 U. S. 1; Cooper, etc., Co. v. Ferguson, 113 U. S. 727; Pembina, etc., Co. v. Pennsylvania, 125 U. S. 181; People, etc., Co. v. Wemple, 131 N. Y. 64; Norfolk R. Co. v. Pennsylvania, 136 U. S. 114; McCall v. California, 136 U. S. 104; Gloucester, etc., Co. v. Pennsylvania, 114 U. S. 196; Robbins v. Shelby Taxing District, 120 U. S. 489.

poration, by which the former is to canvass certain territory for the sale of its sewing machines which are to be sold to him on credit, and a bond given the corporation to secure payment, is an act of interstate commerce, and not affected by a statute prohibiting business within the state by a foreign corporation which has not complied with certain requirements.[1]

A law requiring every foreign building and loan association to pay an annual tax of two per cent. on its gross receipts is not an interference with commerce among the states.[2] The foreign corporation can not complain if it is subjected to a tax which is not imposed upon domestic corporations.[3] The sale and setting up of machinery by a corporation in a state in which it has no agency, is an act of interstate commerce.[4]

§ 251. **Insurance not interstate commerce.**—A large part of the litigation which has arisen as a result of the foregoing rules has grown out of the business of insurance, which is to such a great extent transacted by foreign corporations. It is settled law that the business of insurance, when conducted between citizens of a state and a foreign corporation is not interstate commerce,[5] and, hence, a state may prescribe the conditions upon which insurance companies, created under the laws of other states, may do business within the state.[6] Thus, a foreign insurance campany may be required to make a deposit with some state officer for the purpose of securing persons who contract with it.[7] So it may require that the agent of a foreign insurance company shall retain money of the company until a loss of which he has notice is paid.[8] Such corporations have

[1] Gunn v. White, etc., Co., 57 Ark. 24, 18 L. R. A. 206.

[2] Southern, etc., Assn. v. Normon, 98 Ky. 294, 31 L. R. A. 41.

[3] Liverpool, etc., Co. v. Massachusetts, 10 Wall. (U. S.) 566; Tatem v. Wright, 23 N. J. L. 429; People v. Wemple, 131 N. Y. 64.

[4] Milan, etc., Co. v. Gorten, 93 Tenn. 590, 26 L. R. A. 135.

[5] Crutcher v. Kentucky, 141 U. S. 47; Paul v. Virginia, 8 Wall. 168.

[6] State v. Phipps, 50 Kan. 609, 18 L. R. A. 657.

[7] Paul v. Virginia, 8 Wall. (U. S.) 168.

[8] Phœnix, etc., Co. v. Burdett, 112 Ind. 204.

no right to exercise franchises and privileges in a state contrary to the law of the state, and may be ousted from the exercise of such forbidden privileges by *quo warranto*,[1] although it may have obtained a license to do business in the state from the insurance commissioner.[2]

§ 252. **No visitorial power over foreign corporations.**—The courts of a state will not exercise visitorial power over or interfere with the management of the internal affairs of a foreign corporation.[3] No such power exists unless expressly conferred by statute.[4] A court will not interfere with the internal management of a foreign corporation at the suit of a resident stockholder by setting aside unwise contracts which depreciate and destroy the value of the stock, although the visible and tangible property of the corporation, consisting of conduits in streets for electric lighting is within the state.[5] But a foreign corporation which does business in a state may be compelled by mandamus to produce its books which are kept in another state, for inspection by a stockholder.[6] A statute granting powers and privileges to corporations must be construed to apply only to corporations over which it has the power of visitation.[7]

§ 253. **Right to compel issue of a new stock certificate.**—A state may compel a foreign corporation which is doing business within its borders to issue to a resident shareholder a new certificate of stock in place of one which has been lost. In a case where this was done the court said:[8] "The doctrine is well

[1] State v. Fidelity, etc., Co., 49 Ohio St. 440, 16 L. R. A. 611; State v. Western, etc., Co., 47 Ohio St. 167, 8 L. R. A. 129.

[2] State v. Fidelity, etc., Co., 49 Ohio St. 440, 16 L. R. A. 611.

[3] Clark v. Mutual, etc., Assn. (D.C.), 43 L. R. A. 390; Guilford v. Western Union, etc., Co., 59 Minn. 332; Mining Co. v. Field, 64 Md. 151, 20 Atl. Rep. 1039; Smith v. Insurance Co., 14 Allen 336.

[4] Republican, etc., Mines v. Brown, 19 U. S. App. 203, 58 Fed. 644, 24 L. R. A. 776.

[5] Madden v. Penn., etc., Co., 181 Pa. St. 617, 38 L. R. A. 638.

[6] State v. Swift, 7 Houst. (Del.) 137.

[7] Re Prime Estate, 136 N. Y. 347, 18 L. R. A. 713.

[8] Guilford v. Western Union, etc., Co., 59 Minn. 332, 61 N. W. Rep. 324.

settled that courts will not exercise visitorial powers over foreign corporations, or interfere with the management of their internal affairs. Such matters must be settled by the courts of the state creating the corporation. This view rests upon a broader and deeper foundation than the want of jurisdiction in the ordinary sense of that word. It involves the extent of the authority of the state (from which its courts derive all their powers) over foreign corporations. The only difficulty is in drawing the line of demarkation between matters which do and those which do not pertain to the management of the internal affairs of a corporation. To entertain an action to dissolve a corporation, to determine the validity of its organization; to determine which of two rival organizations is the legal one, or who of rival claimants are its legal officers; to restrain it from declaring a dividend, or to compel it to make one; to restrain it from issuing its bonds, or from making an additional issue of stock,—would clearly all be the exercise of visitorial powers over the corporation, or an interference with the management of its internal affairs. But the distinction between any of these cases and the one at bar seems to us very apparent. * * * We think there are cases, and that this is one of them, where, although the rights of a party grow out of his membership in the corporation, yet, as the matter affects only his individual rights under the contract by which the stock was issued, therefore an enforcement of those rights will not be an interference with the internal management of the corporate affairs within the meaning of the rule.

"If, upon principles of law or comity, foreign corporations are allowed to do business and maintain suits in another state, the general rule should be that they are liable to be sued in the same jurisdiction. Their rights and liabilities in that regard ought to be reciprocal. If we recognize their existence for one purpose, we ought also for the other. If our courts admit and vindicate their rights, justice requires that we also enforce their liabilities, and that, before we send our own citizens to a foreign jurisdiction for redress, it should be very clear that the subject of the action is beyond the limits of the power

or sovereignty of the state over the foreign corporation. If a citizen of this state held a certificate of stock in a foreign corporation, which was alleged to have been illegally issued, or to have for some cause become forfeited, we do not think there would be any doubt but that our courts would entertain a suit by the corporation to compel its surrender and cancellation."

III. The Rule of Comity.

§ 254. **The comity of states.**—The doctrine of comity which is universally recognized among independent states[1] applies with peculiar force to the states of the Union. Formerly a mere matter of international benevolence and courtesy it is now recognized as an obligation.[2] The courts of one state will assume the legal existence of a foreign corporation,[3] and in the absence of a legislative expression of a contrary policy will recognize the right of the corporation to do business in the state. It is the comity of the state and not of the court which is awarded, and the court can not impose conditions upon the corporation.[4] If the corporation was legally created in the state of its origin its corporate capacity will be recognized everywhere, but if not legally created it can not cure the defect by migration.[5] The law of comity is a part of our common law.[6]

[1] Comity is the foundation of private international law. Dr. Woolsey says: "The foundation of this department, as of all privileges granted to strangers, is not generally regarded as being justice in the strict sense, but the humanity and comity of nations, or in other words, the recognition of the brotherhood of men, and the mutual duties thence arising. Justice may close the avenues of commerce, and insist that the most rigid notion of sovereignty be carried out in practice, but good will grants concessions to aliens, and meanwhile enlightened self-interest discovers that the interests of all are promoted." See language of Davis, J., in Merrick v. Van Santvoord, 34 N. Y. 208.

[2] See Calvo, LeDroit Int. II, § 537; Story's Conf. of Laws, § 38; Wheaton Elem. (Dana), p. 134; (Lawrence) p. 162.

[3] Statutes extending the legal existence of corporations a certain time after dissolution for the purpose of suits and forbidding the defense of want of legal organization of the corporation, do not apply to corporations of other states. Marion, etc., Co. v. Perry, 74 Fed. Rep. 425, 41 U. S. App. 14, 33 L. R. A. 252.

[4] Story's Conf. of Laws, § 38.

[5] Demarest v. Flack, 128 N. Y. 205.

[6] Elston v. Piggott, 94 Ind. 14.

§ 255. **The general rule.**—By virtue of the law of comity it is settled that where a state does not forbid or its public policy, as evidenced by its laws, is not infringed, a foreign corporation may transact business within its boundaries and be entitled to the protection of its laws.[1] As said in a New York case,[2] unless the legislature forbids it, foreign corporations can come here as freely as natural persons and exercise here all the powers conferred upon them by their charter, subject to the limitations imposed upon natural persons, that is, they can do no act in violation of our laws or our public policy. But, unless prohibited by law, they can do here, within the limits of their chartered powers, precisely what domestic corporations can do. The rule is thus stated by Mr. Justice Harlan:[3] "In harmony with the general law of comity obtaining among the states composing the Union, the presumption should be indulged that the corporation of one state not forbidden by the law of its being may exercise within any other state the general powers conferred by its own charter unless it is prohibited from so doing either in the direct enactments of the latter state or by its public policy to be deduced from the general course of its legislation, or from the settled adjudications of the highest courts." This rule is, however, subject to the following exceptions: A state will not permit a foreign corporation to exercise within its limits any extraordinary franchise

[1] People v. Fire Assn. of Philadelphia, 92 N. Y. 311, 44 Am. Rep. 380.

[2] Hollis v. Drew Theolog. Seminary, 95 N. Y. 166; Lancaster v. Amsterdam, etc., Co., 140 N. Y. 576, 24 L. R. A. 322.

[3] Christian Union v. Yount, 101 U. S. 352. A foreign corporation may hold real estate in another state unless the right is denied it by its charter or the law of such other state. The right will be granted by the law of comity. Lancaster v. Armstrong, etc., Co., 140 N. Y. 576, 24 L. R. A. 322, annotated; Runyon v. Coster, 14 Pet. (U. S.) 122; Lumbard v. Aldrich, 8 N. H. 31, 28 Am. Dec. 381; Lathrop v. Commercial Bank, 8 Dana (Ky.) 114, 33 Am. Dec. 481; Santa Clara Female Academy v. Sullivan, 116 Ill. 375; Claremount, etc., Co. v. Royce, 42 Vt. 730. The power of the corporation to hold real estate will be presumed, at least, in favor of its grantee. Tarpey v. Deseret, etc., Co., 5 Utah 495. May take a lease or mortgage on real estate. Lebanon Sav. Bank v. Hollenbeck, 29 Minn. 322; Black v. Caldwell, 83 Fed. Rep. 880. The right of a foreign corporation to own water-works in the state can only be questioned by the state. United, etc., Co., v. Omaha, etc., Co., 48 N. Y Supp. 817, citing cases.

or privileges to which it may be entitled under its charter such as exemption from taxation, or the right of eminent domain, or to do any acts contrary to the laws or public policy of the state or not authorized by the charter of the corporation.

§ 256. **Contracts contrary to the law of the forum.**—As a general rule, a state will enforce rights not in their nature local and not contrary to its public policy wherever arising, without regard to whether they are of statutory or common law origin.[1] But comity does not require the enforcement of contracts which are against public policy,[2] injurious to public rights, offensive to morals or contrary to law.[3] The powers sought to be exercised must be in harmony with the general policy of the state. Hence, a foreign corporation will not be permitted to do acts within a state which are prohibited by the law of the state to its own citizens or to corporations engaged in a similar business. Comity does not require that non-residents shall be allowed a remedy which the policy of the state denies to its own citizens.[4] The law of the forum governs in all matters relating to the remedy.[5] A mercantile corporation can not carry on its business in a state which prohibits the organization of such corporations.[6] Special privileges which a foreign corporation enjoys under its charter can not be exercised beyond the boundaries of the state by which it is created, especially when such privileges are contrary to the policy of the other jurisdiction.[7] A foreign corporation can not exer-

[1] Usher v. West Jersey R. Co., 126 Pa. St. 206, 4 L. R. A. 261; Boston, etc., Co. v. Coffin, 152 Mass. 95, 8 L. R. A. 740; Bullard v. Chandler, 149 Mass. 532, 5 L. R. A. 104; Heiskell v. Chickasaw Lodge, 87 Tenn. 668, 4 L. R. A. 699.

[2] Faulkner v. Hyman, 142 Mass. 53; Beard v. Basye, 7 B. Mon. 133; Fenton v. Livingston, 3 Macq. H. L. 497.

[3] Seamans v. Temple Co., 105 Mich. 400, 28 L. R. A. 430; Jones v. Surprise, 64 N. H. 243; Pope v. Hanke, 155 Ill. 617, 28 L. R. A. 568; Gooch v. Faucette, 122 N. C. 270, 39 L. R. A. 835; Emery v. Burbank, 163 Mass. 326, 28 L. R. A. 57.

[4] Ruhe v. Buck, 124 Mo. 178, 25 L. R. A. 178.

[5] Eingartner v. Illinois, etc., Assn., 94 Wis. 70, 34 L. R. A. 503.

[6] Empire, etc., Co. v. Alston, etc., Co., 4 Tex. App., Civ. Cas. 346, 12 L. R. A. 366.

[7] Falls v. United States, etc., Assn., 97 Ala. 417, 24 L. R. A. 174, the court said: "The statutes of Minnesota have no binding force with us, and any provision found in them which authorizes a corporation of their creation

cise the right of eminent domain unless expressly granted to it by the state in which it is doing business.[1]

§ 257. **Public policy, how determined.**—It is not always easy to determine when an act is contrary to the public policy of the state. An act which a state permits its own corporations to do can not be considered as contrary to the public policy of the state.[2] The prohibition by the New York statute of assignments by domestic corporations for the benefit of creditors is held not to show a public policy of the state which will prevent a foreign corporation having property in the state from exercising its common-law right to make such an assignment, especially when the assignment is valid in the state of the creation of the corporation.[3] In order to discover the public policy of a state it is necessary to examine its constitution, its laws and judicial decisions.[4]

§ 258. **Discrimination against non-residents.**—A foreign corporation will not be permitted by the law of comity to enforce a contract which would result in giving the citizens of another state an advantage over residents. But the mere fact

to contract for and recover more than eight per cent. for the loan or forbearance of money is obnoxious to our statute for the prevention of usury. We hold further that the contract which gave rise to the present suit is an obnoxious contract, and can only be enforced to the extent our statute permits. Any statute of this state which may be supposed to confer on building and loan associations the right to charge more than eight per cent. interest, even if we conceded such statutory authority, must be confined in its operation to such corporations as are chartered in Alabama." This decision is manifestly a wrong application of a correct rule. The contract was a Minnesota contract, and should have been governed by the Minnesota laws. It is, also, very difficult to see why the provision, with reference to the rate of interest, was contrary to the law or public policy of Alabama which authorized the creation of similar corporations with the same privileges. As to usury in building and loan association contracts, see the case of Reeve v. Ladies', etc., Assn., 56 Ark. 335, 18 L. R. A. 129, and cases cited in an extensive note, and Rhodes v. Missouri, etc., Assn., 173 Ill. 621, 42 L. R. A. 93.

[1] Holbert v. St. L., etc., R. Co., 45 Iowa 23.

[2] American Union v. Yount, 101 U. S. 352.

[3] Vanderpoel v. Gorman, 140 N. Y. 563, 24 L. R. A. 548.

[4] Girard Will Case, 2 How. (U. S.) 127; Lancaster v. Amsterdam, etc., Co., 140 N. Y. 576, 24 L. R. A. 322.

that a foreign corporation has authority to carry on a business not granted to domestic corporations will not prevent the foreign corporation from doing business in the state. Thus, multiform insurance may be carried on by a foreign corporation, in a state whose domestic corporations are not authorized to do so, if there is no express prohibition by statute.[1] A charter privilege as to the rate of interest a corporation may receive will not be recognized in another state when the local usury laws expressly deny the right to domestic corporations.[2] In a recent case,[3] a Missouri corporation loaned money upon a mortgage on real estate situated in Illinois. The corporation was a legally organized building and loan company under the laws of Missouri, and had authority to procure money for loaning by selling its paid-up shares. This privilege was not granted to similar corporations organized under the laws of Illinois. The Illinois courts refused to grant to the corporation the rights of an Illinois building and loan company, and treated it as an ordinary loan company; and, as such, not exempt from the usury laws of Illinois. Had the corporation not possessed powers which, in the judgment of the Illinois court, deprived it of the character of an Illinois building and loan corporation, its claim of exemption from the usury laws would doubtless have been admitted, as such exemptions were granted domestic building and loan corporations by the Illinois law. The court said: "The rules of comity among states are so liberal that if it should appear to us that an association is engaged in doing business under statutes similar in all respects to our own, we should apply to it the same rules as are applicable to associations organized under our own statutes. * * * Under the general rule of comity existing between states, we will allow to foreign corporations a standing in our courts to enforce the valid contracts they may have made with our citizens, and all valid liens against property

[1] People v. Fidelity, etc., Co., 153 Ill. 25, 26 L. R. A. 295. See Vanderpoel v Gorman, 140 N. Y. 563.

[2] Falls v. United States, etc., Assn., 97 Ala. 417, 24 L. R. A. 174.

[3] Rhodes v. Missouri, etc., Assn., 173 Ill. 621, 42 L. R. A. 93; Meroney v. Atlantic, etc., Assn., 112 N. C. 842.

situated in this state. But that rule of comity does not require that we should allow foreign corporations to enforce contracts here if such enforcement would be in conflict with our laws, and, being thus in conflict, the enforcement whereof would work against our own citizens, and give to the citizens of another state an advantage which the resident has not.[1] As has been said by this court,[2] comity between different states does not require a law of one state to be executed in another when it would be against the public policy of the latter state. No state is bound to recognize or enforce contracts which are injurious to the welfare of its people, or which are in violation of its own laws.[3] If, therefore, it appears that the state of Illinois has granted to corporations of this state certain rights and privileges, and immunity from penalties provided in certain other sections of our statute, and a foreign corporation attempts to invoke the aid of the courts of this state to the same extent, it must affirmatively appear that such foreign corporation is organized and doing business under a similar statute before it will be entitled to like consideration; and where it clearly appears, as it does in this case, that the amount received by a foreign corporation as compensation for its loan or advancement is far in excess of the legal rate of seven per cent. allowed by our statute, then it must affirmatively appear that the statute under which such corporation is organized is identical with, or at least substantially like, our own."

§ 259. **Acts not authorized by charter.**—It is well settled that the doctrine of comity does not require a state to permit a foreign corporation to exercise powers which it is not authorized to exercise by its charter. "The contract must be one which the foreign corporation is permitted by its charter to make."[4] Charter restrictions follow a corporation and are operative wherever it does business.[5] Thus, a corporation

[1] Walters v. Whitlock, 9 Fla. 86.

[2] Pope v. Hanke, 155 Ill. 617, on page 628, 28 L. R. A. 568.

[3] Story, Confl. L., § 327; Faulkner v. Hyman, 142 Mass. 53; Hill v. Spear, 50 N. H. 253, 9 Am. Rep. 205; Fisher v. Lord, 63 N. H. 514.

[4] Bard v. Poole, 12 N. Y. 495; Morris v. Hall, 41 Ala. 510.

[5] American, etc., Co. v. Farmers',

which is not by its charter permitted to hold real estate, will not be permitted to hold real estate in a state other than that by which the charter was granted.[1]

§ 260. **Restrictions imposed by general law.**—A distinction is sometimes made between limitations upon corporate powers which are imposed by a general law and such as are contained in a charter. A limitation contained in a charter is operative everywhere. But only general limitations which are intended to adhere in the constitution of the corporation, and to apply to all acts wherever done, are, as a rule, recognized in other states.[2] It has been said that a court would recognize in a foreign jurisdiction only those powers and capacities which would be recognized by the courts of the state incorporating it, if they were considering the particular act in question.[3] The New York statute prohibiting assignments by insolvent corporations was held to have no extra-territorial force, and not to affect the validity of an assignment by an insolvent corporation made in Ohio of property situated in Illinois.[4] In New York it was held that the power of a Pennsylvania corporation to take under a New York will was restricted by a Pennsylvania statute which forbade gifts by a will executed under certain circumstances.[5] But the weight of authority seems to sustain the view that such statutes are directed to the individuals, and not to corporations. In Ohio it was held that a New York statutory prohibition against a devise to a corporation did not prevent a New York corporation from taking a devise of real estate situated in Ohio, if the terms of its charter were broad enough to authorize it to hold land.[6] In Massachusetts

etc., Co., 20 Colo. 203, 25 L. R. A. 338; Blair v. Perpetual, etc., Co., 10 Mo. 559, 47 Am. Dec. 129; Ohio, etc., Co. v. Merchants', etc., Co., 11 Humph. (Tenn.) 1, 53 Am. Dec. 742.

[1] Diamond, etc., Co. v. Powers, 51 Mich. 145; Hope, etc., Co. v. Perkins, 38 N. Y. 404.

[2] Ohio, etc., Co. v. Merchants', etc., Co., 11 Humph. (Tenn.) 1, 24, 53 Am. Dec. 742.

[3] Christiancy, J., in Thompson v. Waters, 25 Mich. 214.

[4] Warren v. First Nat'l Bank, 149 Ill. 9. See Pairpoint, etc., Co. v. Watch Co., 161 Pa. St. 17.

[5] Kerr v. Dougherty, 79 N. Y. 327.

[6] American, etc., Soc. v. Marshall, 15 Ohio St. 537. See also White v. Howard, 38 Conn. 342; Thompson v. Swoope, 24 Pa. St. 474; *contra*, House of Mercy v. Davidson, 90 Tex. 529.

it was held that the New York statute which prohibited any person from devising more than one-half of his estate to a religious association or corporation did not apply to a devise to such a New York corporation by a non-resident of property situated in another state. The court said: "It seems to us that the statute of New York was intended to apply only to testators who were inhabitants of that state. It is not an act relating primarily to corporations, or designed primarily to limit the amounts they may receive; but it is an act relating to wills, and designed for the protection or benefit of persons interested in the estates of inhabitants of that state. There is nothing in it to prevent a New York corporation from receiving any bequests which may be made to it by an inhabitant of another state, and which may be lawful according to the laws of the place of his residence."

IV. Statutory Restrictions.

§ 261. **In general.**—Almost all of the states have modified the rule of comity as to the recognition of foreign corporations, and adopted statutes designating the conditions upon which such corporations may transact business. These statutes contain many features in common and have for their general purpose the protection of the people of the state from the acts of irresponsible foreign corporations. They generally provide for the granting of licenses to foreign corporations upon their complying with prescribed conditions; and require that the corporation shall maintain an office within the state, and designate some agent upon whom service of process may be made.[1]

[1] Stimson, Am. St. Law, II, ch. iv, §§ 8400-8499. As to such restrictions, see People v. Fidelity, etc., Co. (Ill.), 26 L. R. A. 295, and note to State v. Ackerman (Ohio), 24 L. R. A. 296. The Michigan statute relating to the incorporation of domestic manufacturing and mercantile corporations, which provides that foreign corporations organized for any of the purposes contemplated by said act, upon recording copies of their articles of association and appointing a resident agent for service of process, may carry on business in the state and enjoy all the rights and privileges and be subject to all the restrictions and liabilities of corporations existing under said act, does not prohibit foreign corporations from doing business in the state until they have complied with such conditions, or invalidate contracts made by

A statute which admits corporations of a certain kind impliedly excludes those organized for other purposes.[1]

§ 262. **Conditions which may be imposed.**—From the general power of the state to exclude foreign corporations, it follows that, subject to the restrictions imposed by the national constitution, it is the sole judge of the conditions upon which foreign corporations may be permitted to do business within the state. A statute imposing conditions must stand unless it is clearly unconstitutional.[2] It is immaterial whether the conditions imposed are reasonable or unreasonable.[3] It is no objection to such a condition that it results in a discrimination in favor of domestic corporations. Thus, a foreign corporation may be discriminated against in the matter of taxation,[4] and a foreign corporation may be required to pay a higher license than is required of domestic corporations.[5]

A state may impose a franchise or a license tax on a foreign corporation for the privilege of doing business.[6] An act taxing foreign insurance companies for the benefit of a firemen's fund is constitutional.[7] Foreign corporations selling goods in Michigan by traveling salesmen are not required to pay the franchise fee required of domestic corporations. The act if applied to

them. It simply prescribes the terms upon which such corporations, if they so desire, may become entitled to the benefits of the act conferred upon domestic corporations of similar character. People v. Hawkins, 106 Mich. 479.

[1] Isle Royal, etc., Corp. v. Secretary of State, 76 Mich. 162.

[2] Phœnix, etc., Co. v. Burdett, 112 Ind. 204; State v. Carey, 2 N. Dak. 36; State v. Phœnix, etc., Co., 92 Tenn. 420.

[3] Hartford, etc., Co. v. Raymond, 70 Mich. 485.

[4] Phœnix, etc., Co. v. Com., 5 Bush (Ky.) 68, 96 Am. Dec. 331; Atty.-Gen'l v. Bay State, etc., Co., 99 Mass. 148; Liverpool, etc., Co. v. Mass., 10 Wall 566; People v. Thurber, 13 Ill. 554; Western Union, etc., Co. v. Lieb, 76 Ill. 172; Phœnix, etc., Co. v. Burdett, 112 Ind. 204. The conditions must be imposed by the legislature and not by the courts. Demarest v. Flack, 128 N. Y. 205.

[5] Insurance Co. v. New Orleans, 1 Woods 85; Pembina, etc., Co. v. Pennsylvania, 125 U. S. 181. When the statutes require the corporation to file an instrument designating its place of business within the state, it is sufficient to name the city in which its office is located. McLeod v. American, etc., Co., 100 Ala. 496, 14 So. Rep. 409.

[6] Commonwealth v. Standard, etc., Co., 101 Pa. St. 119.

[7] Trustees v. Roome, 93 N. Y. 313.

such corporations would impose an illegal restraint upon interstate commerce.[1]

§ 263. **Retaliatory statutes.**—The courts have generally sustained the validity of statutes which authorize foreign corporations to do business within the state upon such terms and conditions as are, or may be, imposed upon the corporations of the enacting state in the state of the domicile of the foreign corporation in question.[2] It has been contended that such statutes are unconstitutional, as an abdication by the legislature of its functions and a delegation of its powers to a foreign legislature. But such a statute is a complete law which is to go into effect upon the happening of a contingency and is not an abandonment of the legislative functions.[3] Such a provision is "a constitutional and valid exercise of legislative will, is not void for uncertainty, is susceptible of enforcement, and ought to be enforced upon the happening of the contingency therein mentioned."[4] Under a statute, sec. 29, chap. 73, Rev. Statute of Illinois, 1874, which provides that its provisions shall go into effect "when, by the laws of any other state, any * * * prohibitions are imposed or would be imposed on insurance companies of this state doing or which might seek to do business in such other state," the mere existence of the law in another state is sufficient to put the retaliatory law in force.[5] But

[1] Wilcox, etc., Co. v. Mosher (Mich.), 72 N. W. 117.

[2] State v. Fidelity, etc., Co., 39 Minn. 538; Home, etc., Co. v. Swigert, 104 Ill. 653; Germania, etc., Co. v. Swigert, 128 Ill. 237, 4 L. R. A. 473; State v. Insurance Co., 115 Ind. 257; Phœnix, etc., Co. v. Walch, 29 Kan. 672; People v. Fire Assn. of Philadelphia, 92 N. Y. 311; Goldsmith v. Home, etc., Co., 62 Ga. 379; State v. Insurance Co. (1892), 49 Ohio St. 440, 16 L. R. A. 611; Talbott v. Fidelity, etc., Co., 74 Md. 536, 13 L. R. A. 584.

[3] Home, etc., Co. v. Swigert, 104 Ill. 653; Alcorn v. Hamer, 38 Miss. 652; State v. Parker, 26 Vt. 357.

[4] State v. Insurance Co., 115 Ind. 257.

[5] Germania, etc., Co. v. Swigert, 128 Ill. 237, 4 L. R. A. 473. "It is not important nor necessary to the existence of the law here that an Iowa company should go to New York to test the sincerity of the people in the enforcement of her law; nor is such a step necessary to the enforcement of the law in this state. A spirit of comity between the states should induce a belief that their laws are made in good faith, and for observance." State v. Fidelity, etc., Co., 77 Iowa 648; Talbott v. Fidelity, etc., Co., 74 Md. 536, 13 L. R. A. 584, 22 Atl. Rep. 395.

in Ohio it was held that to make a case for the application of the retaliatory provision it must appear that an Ohio company had been formed for the purpose of doing substantially the same kind of business in the foreign state, and that it would then be subjected to burdens not imposed by the laws of Ohio upon foreign corporations.[1] Such statutes will not be enforced against a foreign corporation unless it is clearly proved that they would have the restrictive effect which is claimed.[2]

§ 264. **Waiver of constitutional rights—Removal of causes.** —There has been some conflict among the courts as to the right of a state to require of a foreign corporation as a condition precedent to the right to do business, a stipulation not to remove to the federal courts actions which may be commenced against it in the state courts. The state courts have generally sustained such provisions. Under the decisions of the federal courts they are unconstitutional. The question arose in Wisconsin, and the court held the provision valid. Upon appeal to the supreme court of the United States, the decision of the supreme court of Wisconsin was reversed.[3]

Subsequently the supreme court of Wisconsin held that although the provision was not binding upon the corporation the state might revoke the license, if the corporation chose to insist upon its constitutional right to litigate in the federal courts. Chief Justice Ryan said:[4] "The statute extended to these foreign insurance companies the privilege of doing business in this state on equal footing with domestic corporations. Experience showed their power to harass the citizens of the state doing business with them by removing actions on their policies from courts of the vicinage to distant and expensive tribunals. Hence the provisions of the statute; and conceding to the fullest extent the right of removal of actions

[1] State v. Insurance Co., 49 Ohio St. 440, 16 L. R. A. 611.

[2] People v. Fidelity, etc., Co., 153 Ill. 25, 26 L. R. A. 295; State v. Insurance Co., 49 Ohio St. 440, 16 L. R. A. 611; State v. Fidelity, etc., Co., 39 Minn. 538.

[3] Insurance Co. v. Morse, 20 Wall. 445. See Lafayette, etc., Co. v. French, 18 How. (U. S.) 404; Commonwealth v. Coal Co., 97 Ky. 238.

[4] State v. Doyle, 40 Wis. 175.

commenced, we can see no pretense for questioning the power of the state, in the exercise of its absolute discretion on the subject, to revoke the license of the company exercising the right. The state has the power to make its voluntary license subject to the forbearance of a right, and revokable upon its exercise. The right may survive the license, but the license can not survive its exercise. So grants are sometimes made upon conditions to forbear a right. It was for the authorities of the state alone to judge that the exercise of the right was an abuse of the privilege of the license, * * * the federal courts * * * have no jurisdiction over the question whether foreign corporations, exercising the right, shall be permitted by the state to do business within it. That is a matter of state policy, state law, state jurisdiction."

This decision was approved by the supreme court of the United States,[1] but in a later case[2] it was held that where the statute provided that no permit should be granted to a foreign corporation until a stipulation was entered into that it would not remove actions brought against it to the federal courts, it was apparent that the purpose was to deprive the corporation of its constitutional rights and that the statute was void. In a still later case the court said: "But that statute requiring the corporation, as a condition precedent to obtaining a permit to do business within the state, to surrender a right and privilege secured to it by the Constitution and laws of the United States, was unconstitutional and void, and could give no validity or effect to any agreement or action of the corporation in obedience to its provisions."[3] But the fact remains that the state may entirely exclude the corporation if it chooses to stand on its constitutional right. A person may waive a constitutional provision in his favor.[4]

[1] Doyle v. Insurance Co., 94 U. S. 535.

[2] Barron v. Burnside, 121 U. S. 186. This case arose on a prosecution of an agent of the corporation for engaging in the business of the corporation which had not obtained a license as required by statute of Iowa.

[3] Southern, etc., Co. v. Denton, 146 U. S. 202; Texas, etc., Co. v. Worsham, 76 Tex. 556.

[4] Embury v. Conner, 3 N. Y. 511; In re Cooper, 93 N. Y. 507.

§ 265. **The granting and revocation of a license.**—Statutes generally provide that the license to do business shall be granted by some state officer, upon application by the corporation and compliance with the statutory conditions. Whether the action of this officer is judicial or administrative depends upon the language of the statute.[1] If it is apparent that no discretion was intended to be vested in the officer, but that he should grant the license when the conditions are complied with, his acts are ministerial and subject to the control of the courts,[2] but if it is apparent that the legislature intended that the officer should exercise judgment and discretion, in granting or revoking a license, his acts are judicial and not subject to the control of the courts.[3] The state is not estopped from insisting upon compliance with a condition by the failure of its officials to require compliance at the proper time.[4] If a corporation is so organized that it is impossible for it to comply with the conditions imposed by the restrictive statute, it can not compel the issue of a license to it.[5] The motives which induce a state to exclude a foreign corporation or authorize the revocation of a license are immaterial, and can not be made the subject of a judicial inquiry.[6]

§ 266. **Meaning of "doing business."**—These words as used in the various statutes refer to the general transaction of business, and not to an isolated transaction, without the intention of continuing business.[7] Thus, it does not include a mere con-

[1] Lafayette, etc., Co. v. French, 18 How. 404; Ducat v. Chicago, 10 Wall. 410; Insurance Co. v. Morse, 20 Wall. 445; St. Clair v. Cox, 106 U. S. 350; Philadelphia, etc., Assn. v. New York, 119 U. S. 110.

[2] State v. Fidelity, etc., Co., 39 Minn. 538.

[3] Travelers, etc., Co. v. Fricke (Wis., 1898), 41 L. R. A. 557; State v. Doyle, 40 Wis. 175, 22 Am. Rep. 692; State v. Carey, 2 N. Dak. 36, 49 N. W. Rep. 164; Dwelling-House, etc., Co. v. Wilder, 40 Kan. 561; Kansas, etc., Co. v. Wilder, 43 Kan. 731; Isle Royal, etc., Co. v. Osmun, 76 Mich. 162.

[4] Travelers, etc., Co. v. Fricke (Wis.), 41 L. R. A. 557.

[5] Mutual, etc., Co. v. House, 89 Tenn. 438; Mutual, etc., Co. v. Swigert, 120 Ill. 36, 11 N. E. Rep. 410; Isle Royal, etc., Co. v. Osmun, 76 Mich. 162.

[6] Doyle v. Continental, etc., Co., 94 U. S. 535.

[7] Cooper, etc., Co. v. Ferguson, 113 U. S. 727; Tabor v. Goss, etc., Co., 11 Colo. 419; Farmers', etc., Co. v. Lake, etc., R. Co. (Ill.), 51 N. E. Rep. 55.

signment of goods by a foreign corporation to a citizen of the state,[1] nor the purchase of an article of machinery within the state,[2] nor the sale of milling machinery and placing it in a mill by a corporation which has no office in the state,[3] nor soliciting subscriptions to a newspaper published in a foreign state,[4] nor selling goods by a traveling salesman,[5] nor the frequent purchase of material within the state,[6] nor the investing in the securities of a domestic corporation,[7] nor soliciting subscriptions to the stock of a foreign corporation,[8] nor the appointment of agents who are to transact the business,[9] nor the bringing of a suit.[10] The mere collection of a debt after the passage of an act imposing certain conditions upon the right to do business is not within the prohibition where the debt was due before the passage of the act.[11] The single act by a foreign mortgage loan corporation of lending money upon mortgage security, in Alabama, is held to be "doing business" within the meaning of the law,[12] although the supreme court of

[1] Bertha, etc., Co. v. Clute (N. Y.), 27 N. Y. Supp. 342; Cooper, etc., Co. v. Ferguson, 113 U. S. 727.

[2] Colo. I. Works v. Sierra Grande, etc., Co., 15 Colo. 499; Graham & Anderson v. Hendricks, 22 La. Ann. 523.

[3] Milan, etc., Co. v. Gorten, 93 Tenn. 590, 26 L. R. A. 135.

[4] Beard v. Union, etc., Co., 71 Ala. 60.

[5] Ware v. Hamilton Brown, etc., Co., 92 Ala. 145.

[6] Commonwealth v. Standard, etc., Co., 101 Pa. St. 119.

[7] Gilchrist v. Helena, etc., R. Co., 47 Fed. Rep. 593.

[8] Payson v. Withers, 5 Biss. C. C. 269.

[9] D. S. Morgan & Co. v. White, 101 Ind. 413.

[10] St. Louis, etc., R. Co. v. Phila. Fire Assn., 60 Ark. 325, 28 L. R. A. 83; Utley v. Clark, etc., Co., 4 Colo. 369; Powder River, etc., Co. v. Custer Co., 9 Mont. 145, 22 Pac. Rep. 383; Fuller & Johnson, etc., Co. v. Foster, etc., Co., 4 Dak. 329, 30 N. W. Rep. 166. Upon a contract made out of the state, Barse, etc., Co. v. Rong, etc., Co., 16 Utah 59.

[11] Pioneer, etc., Assn. v. Cannon, 96 Tenn. 599, 33 L. R. A. 112.

[12] Ginn v. New Eng., etc., Co., 92 Ala. 135; Farrior v. New Eng., etc., Co., 88 Ala. 275. See People v. Am. Bell, etc., Co., 117 N. Y. 241. In Reeves v. Harper, 43 La. Ann. 516, it was held that the constitution of Louisiana does not deny to a citizen of Louisiana the privilege of borrowing money from foreign corporations, nor does it prohibit such corporations from loaning money to our citizens, provided only that such transactions are not done in the course of business carried on by the corporation in this state, without complying with the requirements of the constitution. The single act of loaning money within the state is not a doing of business.

A life insurance company chartered

the United States has held otherwise.[1] So in Arkansas it is held that the taking of a single mortgage for a past due debt for goods sold at the demand of the corporation is not doing business in the state.[2]

But a corporation "does business" in a state in which it has an office and sells goods.[3] A corporation which lends money to a resident of the state through a broker domiciled in the state,[4] or in another state,[5] is not doing business in the state.

§ 267. **Contracts made out of the state.**—These restrictive statutes do not affect the right of a citizen of a state to enter

in the state of Illinois carried on business in the state of Missouri through an agent appointed for that purpose. The agent in Missouri would solicit and receive from citizens in that state applications for insurance, which he would forward to the home office of the company in Chicago. When the application was approved the policy was filled in, dated and signed by the officers of the company in Chicago, and transmitted by mail to the agent of the company in Missouri, who, upon the payment to him by the applicant of the first premium, called in this case an entrance fee, delivered the policy to the assured. In Berry v. Knights Templar, etc., Co., 46 Fed. Rep. 439, it was held that the company was doing business in the state of Missouri.

The signing of a policy in Philadelphia by a company located and doing business there and the sending it to the applicant or the attorney of the applicant in New York is not a violation of the New York statute. People v. Imlay, 20 Barb. 68. A foreign corporation organized to act as the general agent of its members in the selling of goods produced by them, and having and employing no capital stock in the state, is not subject to the provision of the statute requiring a statement showing its title, object, location of its offices and names of its agents in the state. Kilgore v. Smith, 122 Pa. St. 48.

[1] Cooper, etc., Co. v. Ferguson, 113 U. S. 727; and see Cæsar v. Capell, 83 Fed. Rep. 403; Pioneer, etc., Co. v. Cannon, 96 Tenn. 599, 33 L. R. A. 112.

[2] Florsheim, etc., Co. v. Lester, 60 Ark. 120, 27 L. R. A. 505. A foreign corporation which has obtained no permit authorizing it to do business in the state may maintain an action in the state court against a non-resident to recover damages under a contract executed and to be performed, except as to the delivery of the property in question, in another state. Ware, etc., Co. v. Anderson, etc., Co. (Iowa, 1899), 77 N. W. Rep. 1026.

[3] People v. Wemple, 131 N. Y. 64; People v. Silver, etc., Co., 105 N. Y. 76.

[4] American, etc., Co. v. Peirce, 49 La. Ann. 390.

[5] American, etc., Co. v. Ogden, 49 La. Ann. 8.

into a contract with a foreign corporation.[1] Thus, when the statute prohibited any person or persons from "paying, receiving or forwarding any premium or application for insurance, or in any manner aiding or helping in the securing or placing of any insurance" with any foreign insurance company not authorized to do business in the state, it was held that the statute applied to persons who, as insurance agents or brokers, do business with unauthorized foreign insurance companies, or agents of other parties, but not to persons who, as owners, make single contracts of insurance with such companies or associations upon their own property. Mr. Justice Mitchell said: "It may be readily conceded that an act which should attempt to prevent a non-resident owner of property in this state, or a resident owner not at the time within its territory, from insuring his property in any manner lawful in the place of the contract, would be void as extra-territorial. So, also, it may be conceded that if a citizen of Pennsylvania has, by a contract validly made outside of its boundaries, incurred a liability, no law of this state can, under the constitution of the United States, prevent his fulfilling that obligation, even by an act done within the state. But beyond the limitations imposed by the constitution, the power of the legislature to declare any acts done within the territory of the state unlawful or criminal can not be questioned; and all considerations of wisdom, of policy, or hardship, of difficulty or even impossibility of general enforcement must be addressed to the law-making branch of the government. We entertain, therefore, no doubt of the power of the legislature to make the insurance of his property in an unauthorized foreign company by an owner criminal, if done in this state; but such a statute would be not only an unusual, but a very harsh and extreme interference with the general right of a citizen to manage his private affairs in his own way. We should not attribute such an intention to the act in question unless its terms be plain or the implication unavoidable."[2]

[1] M. B. Faxon Co. v. Lovett Co., 60 N. J. L. 128.

[2] Com. v. Biddle, 139 Pa. St. 605; Columbia, etc., Co. v. Kinton, 37 N. J.

A contract with a foreign corporation stipulating that it shall not be valid until approved at the principal office of the company, in another state, is not a contract made in the state within the meaning of a statute invalidating contracts made by foreign corporations which have not filed their articles of association and paid the franchise tax.[1]

V. Effect of Failure to Comply With Statutory Requirements.

§ 268. **Effect upon validity of contracts.**—The validity of contracts entered into between citizens of a state and a foreign corporation which has not complied with the conditions precedent to the right to do business in the state is determined by the language of the particular statute. Where the statute expressly declares that such contracts can or can not be enforced there can be no question.[2] Thus, where the statute makes it "unlawful" for an insurance company to do business it can not collect insurance premiums.[3] Generally the statute simply prohibits such corporations from doing business within the state and imposes a penalty upon the corporation or some officer or agent thereof for a violation of this prohibition.

Where the statute provides that a foreign corporation which has not complied with statutory conditions can not *maintain* an action within the state, a motion to dismiss will not be granted where there has been compliance between the time of commencing the action and the hearing of the motion.[4]

The fact that the corporation has not complied with the qualifying statute is not available as a defense when the corporation is sued by a citizen of the state upon a contract entered into by the corporation. The statutes are intended for the protec-

L. 33; Lamb v. Bowser, 7 Biss. C. C. 372; Huntley v. Merrill, 32 Barb. 626; Hyde v. Goodnow, 3 N. Y. 266. In Hooper v. California, 155 U. S. 648, on 656, Mr. Justice White says: The state of California has the right "to prohibit a citizen from contracting within her jurisdiction with any foreign company which has not acquired the privilege of engaging in business therein, either in his own behalf or through an agent empowered to that end." But compare dissenting opinion of Harlan, J.

[1] Holder v. Aultman, etc., Co., 169 U. S. 81.

[2] Neuchatel, etc., Co. v. The Mayor, 30 N. Y. Sup. 252, 155 N. Y. 373; Selser v. Potter, etc., Co., 30 N. Y. Sup. 294; Hartford, etc., Co. v. Matthews, 102 Mass. 221; Conn. River, etc., Co. v. Way, 62 N. H. 622.

[3] Insurance Co. v. Kennedy, 96 Tenn. 711; Hartford, etc., Co. v. Raymond, 70 Mich. 485.

[4] Carson-Rand Co. v. Stern, 129 Mo. 381, 32 L. R. A. 420. After compliance the corporation may enforce a contract previously made. Neuchatel, etc., Co. v. The Mayor, 155 N. Y. 373.

tion of the people and not to enable the corporation to defraud them.[1]

The courts will not hold contracts made by a foreign corporation which has not complied with an enabling statute void unless the legislative intention is clearly expressed in the statute. It will not do so by implication from loose and indefinite language.[2]

§ 269. **Where the statute imposes a penalty.**—The decisions are not uniform, but it seems that the weight of authority supports the proposition that, where a state prohibits a foreign corporation from doing business within its limits, without having first complied with certain conditions, and imposes a penalty for the violation of the statute, the penalty is the sole means contemplated for compelling obedience, and the contract is valid and enforcible.[3] But the provision for a penalty has been held equivalent to an express prohibition of doing business in the state, and to a declaration that contracts made

[1] Pennypacker v. Insurance Co., 80 Iowa 56; Union, etc., Co. v. McMillen, 24 Ohio St. 67.

[2] Elston v. Piggott, 94 Ind. 14; Cæsar v. Capell, 83 Fed. Rep. 403. The Indiana statute against the enforcement in the courts of the state of a contract made by a foreign corporation which does not comply with such statutes does not apply to a suit brought in a federal court to foreclose a mortgage taken upon real estate in Indiana by a building and loan corporation which has not complied with the law. Sullivan v. Beck, 79 Fed. Rep. 200; Hervey v. Railroad Co., 28 Fed. Rep. 169; Farmer, etc., Co. v. Chicago, etc., R. Co., 68 Fed. Rep. 412. The Indiana statute prohibited the enforcement of the contract until compliance. The contract was valid when made and could be enforced after compliance. Maine, etc., Co. v. Cox, 146 Ind. 107.

[3] Kindel v. Beck, etc., Co., 19 Colo. 310, 35 Pac. Rep. 538; Jarvis-Conklin, etc., Co. v. Willhoit, 84 Fed. Rep. 514; Lauter v. Jarvis-Conklin, etc., Co., 85 Fed. Rep. 894, 29 C. C. A. 473; Fritts v. Palmer, 132 U. S. 282; Utley v. Clark-Gardner, etc., Co., 4 Colo. 369; Russell v. Jones, 101 Ala. 261, 13 So. Rep. 145; Toledo, etc., Co. v. Thomas, 33 W. Va. 566; Whitman, etc., Co. v. Strand, 8 Wash. 647; Edison, etc., Co. v. Canadian, etc., Co., 8 Wash. 370; Dearborn, etc., Co. v. Augustine, 5 Wash. 67; Northwestern, etc., Co. v. Overholt, 4 Dillon (C. C.) 287; Am. L., etc., Co. v. East, etc., Co., 37 Fed. Rep. 242; Union, etc., Co. v. McMillen, 24 Ohio St. 67; Pennypacker v. Insurance Co., 80 Iowa 56; Columbus, etc., Co. v. Walsh, 18 Mo. 229; Clay, etc., Co. v. Huron, etc., Co., 31 Mich. 346; Clark v. Middleton, 19 Mo. 53; Ehrmann v. Teutonia, etc., Co., 1 McCrary's 123; Brooklyn, etc., Co. v. Bledsoe, 52 Ala. 538; King v. National, etc., Co., 4 Mont. 1; Wright v. Lee, 4 S. Dak. 237; Washburn, etc., Co. v. Bartlett, 3 N. Dak. 138.

in violation thereof are void.[1] Thus it is held in Pennsylvania that a bond insuring a foreign corporation against the dishonesty of its manager in Pennsylvania is void, and there can be no recovery thereon where the corporation has not complied with the statute requiring the filing of a statement and declaring that any person transacting business for the corporation without compliance shall be guilty of a misdemeanor.[2] If the contract has been fully executed its validity is in no way affected by the failure of the corporation to qualify to do business in the state.[3] There are many cases holding that such contracts are void, on the theory that all acts in violation of a prohibition are void, notwithstanding the provisions for a penalty.[4]

The failure to pay a tax imposed by a statute, not by its terms prohibitory, does not affect the validity of contracts made by the corporation.[5] So where the statute requires certain acts, such as filing a certificate, to be done within a certain time after commencing business, the only penalty for a failure is that imposed by the statute upon the officers.[6]

[1] Ætna, etc., Co. v. Harvey, 11 Wis. 412; Thorne v. Travelers, etc., Co., 80 Pa. St. 15; Mutual, etc., Co. v. Bales, 92 Pa. St. 352.

[2] McCanna, etc., Co. v. Citizens', etc., 76 Fed. Rep. 420, 39 U. S. App. 332, 35 L. R. A. 236. In Longworthy, Receiver, v. Garding (Minn.), 77 N. W. Rep. 207, the court said "that plaintiff can not recover in this proceeding unless the company he represents has complied with the requirements of the statute regulating foreign insurance companies, is not questioned." Citing Seamans v. Christian Bros., etc., Co., 66 Minn. 205. In the latter case it is said "this decision does not conflict with Ganser v. Firemen's Fund Ins., 34 Minn. 372, where it was held that the insured can recover the loss, even though the insurer has not complied with the statutory requirements so as to do business in this state. The very object of these statutory provisions is the protection of the insured, and the parties are not *in pari delicto*."

[3] Gamble v. Caldwell (Ala.), 12 So. Rep. 424.

[4] Cary, etc., Co. v. Thomas, 92 Tenn. 587; Jones v. Smith, 3 Gray 500; Buxton v. Hamblen, 32 Me. 448; Thorne v. Insurance Co., 80 Pa. St. 15; Barbor v. Boehm, 21 Neb. 450; Dudley v. Collier, 87 Ala. 431, 13 Am. St. Rep. 55; Farrior v. New Eng., etc., Co., 88 Ala. 275; Christian v. American Freehold, etc., Co., 89 Ala. 198; Union Central, etc., Co. v. Thomas, 46 Ind. 44; Cassaday v. Amer., etc., Co., 72 Ind. 95; Bank v. Young, 37 Mo. 398; Stewart v. Northampton, etc., Co., 38 N. J. L. 436.

[5] Larned v. Andrews, 106 Mass. 435.

[6] Northwestern, etc., Co. v. Overholt, 4 Dill. (C. C.) 287; Kindel v. Lithograph Co., 19 Colo. 310.

§ 270. **Where no express penalty is provided.**—Where no penalty is provided, it is generally held that such contracts are not enforcible, unless the conditions are such as to give rise to an estoppel. These cases hold that the contract is valid, and that the only penalty for the non-compliance is exclusion from the state,[1] but in other jurisdictions it is held that all contracts entered into in violation of such a statute are unenforcible.[2] "The general rule is that a contract in violation of law is void. The only exception is that when the law imposes a penalty for a prohibited act, and it clearly appears that the legislature intended no more than to impose a penalty for the violation of the law, a contract made in violation of such a statute is not void.[3] We do not think that this statute belongs to the excepted class. The legislature has prohibited the contract and has provided no penalty for its violation. Unless the contract shall be held void, the statute is of no effect." A mortgage, taken before compliance with the statute, was held void, at least as to all but the mortgagor.[4] In a West Virginia case[5] the court said: "We are aware that the courts of Indiana,[6] Illinois,[7] Wisconsin, and perhaps in some other

[1] Wright v. Lee, 4 S. Dak. 237, 55 N. W. Rep. 931; Washburn, etc., Co. v. Bartlett, 3 N. Dak. 138; Slauson v. Schwabacher, etc., Co., 4 Wash. 783.

[2] In re Comstock, 3 Sawyer (U. S.) 218; Cincinnati, etc., Co. v. Rosenthal, 55 Ill. 85; Lycoming, etc., Co. v. Wright, 55 Vt. 526; Ætna, etc., Co. v. Harvey, 11 Wis. 412; Barbor v. Boehm, 21 Neb. 450.

[3] Lester v. Howard Bank, 33 Md. 558; Watrous & Snouffer v. Blair, 32 Iowa 58; Mowing, etc., Co. v. Caldwell, 54 Ind. 270.

[4] Watson, J., in Bank of Columbia v. Page, 6 Ore. 431; Lycoming, etc., Co. v. Wright, 55 Vt. 526; Mowing, etc., Co. v. Caldwell, 54 Ind. 270; Lester v. Howard Bank, 33 Md. 558; National Bank v. Matthews, 98 U. S. 621. In Reliance, etc., Co. v. Sawyer, 160 Mass. 413, 36 N. E. Rep. 59, it was held that a premium note given to a foreign insurance corporation, which had not complied with the statute, could not be enforced. Such a note is without consideration. Haverhill, etc., Co. v. Prescott, 42 N. H. 547. If the contract is void by the law of the state when made it can not be enforced in the courts of another state. Ford v. Buckeye, etc., Co., 6 Bush (Ky.) 133.

[5] Toledo, etc., Co. v. Thomas, 33 W. Va. 566.

[6] The note is not void, but the remedy is suspended. American, etc., Co. v. Wellman, 69 Ind. 413. This is true under the New York statute. Goddard v. Crefeld Mills, 45 U. S. App. 84.

[7] Cincinnati, etc., Co. v. Rosenthal, 55 Ill. 85.

states, hold a different doctrine. In Vermont and Oregon it has been held that a non-compliance with the precedent conditions of the statutes of those states by foreign corporations renders their contracts void. But it will be observed that these statutes imposed no penalty for the failure to comply with their provisions, and it is principally upon this ground that the contracts are held void, because otherwise the statute might be evaded with impunity." Construing the Oregon statute the federal court held that a mortgagor could recover back land taken under foreclosure of a mortgage given to a foreign corporation which had not complied with the statute.[1]

§ 271. **Estoppel to allege non-compliance.**—In some cases it is held that a party who has contracted with a foreign corporation is estopped to question its right to do business in the state.[2] The corporation, if it had power under its charter to enter into the contract in question, is to be regarded as a *de facto* corporation, and a person dealing with it is estopped to deny its authority.[3] But if the contract is regarded as illegal and prohibited, a person dealing with the corporation should be permitted to plead its illegality as a defense.[4] The weight of authority in the state courts supports this rule, although the supreme court of the United States has held that the failure to comply with a statute which declared that no foreign corporation should hold real estate except as provided by statute did not render a conveyance void. The transaction could not, therefore, be attacked by a private person.[5]

In a suit against the corporation there are still stronger reasons for holding that the corporation can not be heard to deny its qualification. There are other cases holding that after enjoying all the benefits of the business and receiving the money of the assured, a corporation will not be heard to say that it

[1] Semple v. Bank of Columbia, 5 Sawyer (U. S.) 88.

[2] Rathbone v. Frost, 9 Wash. 162; Le France, etc., Co. v. Mt. Vernon, 9 Wash. 142; Dearborn, etc., Co. v. Augustine, 5 Wash. 67.

[3] Sherwood v. Alvis, 83 Ala. 115; Wright v. Lee, 2 S. Dak. 596.

[4] In re Comstock, 3 Sawyer (U. S.) 218.

[5] Fritts v. Palmer, 132 U. S. 282.

never submitted to the jurisdiction of the state. It can reap no advantage from its own wrong. To sustain this defense would be to give judicial sanction to business methods much below the standard of common honesty.[1]

§ 272. **Presumption—Burden of proof.**—When the complaint of a foreign corporation is silent on the subject it will be presumed on demurrer that it has complied with the requirements of the statute enabling it to do business in the state.[2] In an action brought by such a corporation it is not incumbent upon it to show that it has complied with the statute and obtained a certificate of authority to do business. Non-compliance with the law is a matter of defense.[3]

VI. Actions By and Against Foreign Corporations.

§ 273. **The right to sue.**—By the rule of comity a corporation may sue in a foreign jurisdiction upon complying with such conditions as are required of non-residents generally, and without complying with the conditions imposed upon foreign corporations doing business within the state.[4] The statutes of a state often grant to foreign corporations the power to sue in its courts. Thus in Minnesota it is provided that a foreign corporation may prosecute in the courts of the state in the same manner as domestic corporations, subject to the limitation that it can not maintain an action upon an obligation

[1] Ehrman v. Insurance Co., 1 Fed. Rep. 471; Fletcher v. Insurance Co., 13 Fed. Rep. 526; Insurance Co. v. Elliott, 5 Fed. Rep. 225; Wall v. Society, etc., 32 Fed. Rep. 273; Insurance Co. v. McMillen, 24 Ohio St. 67; Clay, etc., Ins. Co. v. Huron, etc., Co., 31 Mich. 346; Insurance Co. v. Walsh, 18 Mo. 229; Lamb v. Bowser, 7 Biss. 315, 372; Insurance Co. v. Matthews, 102 Mass. 221; Kilgore v. Smith, 122 Pa. St. 48.

[2] Sprague v. Cutler, etc., Co., 106 Ind. 242; Cassaday v. American, etc., Co., 72 Ind. 95; Nickels v. Building Assn., 93 Va. 380.

[3] Longworthy v. Garding (Minn.), 77 N. W. Rep. 207.

[4] Cone, etc., Co. v. Poole, 41 S. C. 70, 24 L. R. A. 289; Henriques v. Dutch, etc., Co., 2 Ld. Raymond 1532; Spanish Ambassador v. Buntish, Bulst. pt. 2, p. 322; Dutch, etc., Co. v. Moses, 1 Str. 612; Christian v. The American, etc., Co., 89 Ala. 198; McCall v. American, etc., Co., 99 Ala. 427, 12 So. Rep. 806; Utley v. Clark, etc., Co., 4 Colo. 369; Reed v. Walker (Tex., 1893), 21 S. W. Rep. 687; Powder Mill, etc., Co. v. Custer Co., 9 Mont. 145; Christian Union v. Yount,

arising out of, or in consideration of, an act which is contrary to the law or policy of the state or which is thereby forbidden to domestic corporations engaged in a similar business.[1]

The failure of a corporation to comply with a statute regulating the right to do business in a state will not preclude it, or an insurance company subrogated to its rights, from maintaining an action to recover for negligent injuries to its property within the state.[2] A foreign corporation will not be denied the right to sue in the courts of a state merely because its members are all its own citizens.[3]

The courts of equity are not open to a foreign corporation in strict right but as a matter of comity. Jurisdiction will not be taken on service by publication of an action by a foreign corporation having a place of business in the state to recover a debt contracted in another state and not reduced to judgment, from a non-resident whose only property in the state consists of his interest as partner in a firm whose property is practically all in another state where the principal business is carried on.[4]

§ 274. **Actions against foreign corporations.**[5]—Every state may determine for itself whether it will entertain an action

101 U. S. 352; Charter Oak, etc., Co. v. Sawyer, 44 Wis. 387; The American, etc., Co. v. Moore, 2 Dak. 280; Diamond, etc., Co. v. Roeber, 106 N. Y. 473; Day v. Essex Bank, 13 Vt. 97; Newburg, etc., Co. v. Weare, 27 Ohio St. 343; Bank v. Montgomery, 3 Ill. 422; St. Louis, etc., R. Co. v. Fire Assn., 55 Ark. 163; Jewelers', etc., Agency v. Douglass, 35 Ill. App. 627; British, etc., Co. v. Ames, 6 Metc. (Mass.) 391; Libbey v. Hodgdon, 9 N. H. 394; Story Conf. Laws, p. 175, and note; Dicey on Domicile, 198.

[1] Gen. St. 1878, ch. 76, §§ 2, 3. "It is an established rule of private international law that a corporation duly created according to the laws of one state may sue and be sued in its corporate name in the courts of other states. * * * But as regards procedure and parties to actions, the law of the country in which the action is brought prevails." Lindley Partnership, App., p. 1483; Westlake Priv. Int. Law, § 286. See Bar's Priv. Int. Law, § 41, note D.

[2] St. Louis, etc., R. Co. v. Philadelphia, etc., Assn., 60 Ark. 325, 28 L. R. A. 83.

[3] Oakdale, etc., Co. v. Garst, 18 R. I. 484, 23 L. R. A. 639.

[4] National, etc., Co. v. Du Bois, 165 Mass. 117, 30 L. R. A. 628.

[5] As to citizenship for purpose of suit, see St. Louis, etc., R. Co. v. James, 161 U. S. 545, Wilgus' Cases; Shaw v. Quincy Mining Co., 145 U. S. 444, Wilgus' Cases; Barrow S. S. Co. v. Kane, 170 U. S. 100, Wilgus' Cases.

against a foreign corporation. The conditions upon which this will be done are generally determined by statute. Ordinarily such actions will be entertained if the subject of the litigation is such that the court may do complete justice in the matter.[1] A resident stockholder may maintain an action against a foreign corporation to compel it to issue a certificate of stock in lieu of one that has been lost.[2] But a court will not entertain a suit which involves the internal management of foreign corporations.[3] One foreign corporation may sue another foreign corporation in a state where the cause of action arose and both are doing business.[4] A non-resident may sue a foreign corporation doing business in Massachusetts upon a contract made in another state where its subject-matter is located, and make service upon the insurance commissioner, which the company has under the law appointed as its agent to accept service.[5] The relations between a corporation and its shareholders are to be determined by the law of the creating state which will be recognized and applied in the court of a foreign state which has jurisdiction over the action.[6] In Alabama it is held that its courts will not take jurisdiction of an action for personal injuries caused by a Georgia corporation in that state, although part of railroad was operated in Alabama.[7]

§ 275. **Service upon foreign corporations.**—Most of the states have provided statutory methods for service of process upon foreign corporations.[8] At common law service upon a corporation was made by serving upon the principal officer,[9] but the English courts have held that when a foreign corporation

[1] Kansas, etc., R. Co. v. Topeka, etc., R. Co., 135 Mass. 34; New Orleans, etc., R. Co. v. Wallace, 50 Miss. 244.

[2] Guilford v. Western Union, etc., Co., 59 Minn. 332.

[3] Wilkins v. Thorne, 60 Md. 253; Madden v. Electric Light Co., 181 Pa. St. 617.

[4] Emerson T., etc., Co. v. McCormick, etc., Co., 51 Mich. 5, construing a statute.

[5] Johnston v. Trade, etc., Co., 132 Mass. 432; Desper v. Continental Water, etc., Co., 137 Mass. 252; Abell v. Pennsylvania, etc., Co., 18 W. Va. 400.

[6] Bishop v. Globe Co., 135 Mass. 132.

[7] Central R. Co. v. Carr, 76 Ala. 388.

[8] The right to do so is unquestioned. Sparks v. Masonic, etc., Assn., 100 Iowa 458.

[9] Tidd's Prac. (1st Am. ed.), p. 19.

establishes a branch office in England, service upon the agent in charge of such office is good service upon the corporation.[1] In certain early cases it was held that a corporation could only be sued in the state by which it was created by service upon its principal officer within that state, and that statutes providing for service upon corporations have no application to foreign corporations.[2] This rule rested on the theory that service could only be made on the superior officers of the corporation and they could not carry their official capacity with them out of the state.[3] But in other states they are treated as natural non-resident persons, and if proper service can be obtained there is no objection to the court proceeding and determining their rights and liabilities.[4] Service may be made upon the representative of the corporation in the state.[5]

Where a foreign corporation has an office in the state, service may be made upon the head officer in charge of the office when the cause of action arose in the state.[6] But under many of the statutes this can not be done if the cause of action arose in another state.[7]

[1] Newby v. Colts, etc., Co., L. R. 7 Q. B. 293; La Bourgogne, 79 L. T. Rep. 331 (1898-9).

[2] Peckham v. North Parish, 16 Pick. 274; Middlebrooks v. Springfield, etc., Co., 14 Conn. 301; McQueen v. Middleton, etc., Co., 16 John. (N. Y.) 5. "A foreign corporation can only be sued in this commonwealth by means of an attachment of its property; unless, as in the case of a foreign insurance company, by virtue of an express statute." Crafts v. Belden, 99 Mass. 535.

[3] See comment by Justice Field in St. Clair v. Cox, 106 U. S. 350.

[4] Libbey v. Hodgdon, 9 N. H. 394; Railroad Co. v. Harris, 12 Wall. 65, 81; North Mo. R. Co. v. Akers, 4 Kan. 453.

[5] A foreign corporation which enters a state for the transaction of business may be sued by serving process upon its representatives in the state. Van Dresser v. Oregon, etc., Co., 48 Fed. Rep. 202; Nortin v. Berlin Bridge, 51 N. J. Law 442. See note to Foster v. Betcher Lumber Co. (S. Dak.), 23 L. R. A. 490. Statutes often name the character of agents upon whom service may be made. As to who are "managing agents" see Foster v. Betcher Lumber Co. (S. Dak.), 23 L. R. A. 490; as to "local agents," Mexican Central R. Co. v. Pinkney, 149 U. S. 194.

[6] Touchband v. Chicago, etc., R. Co., 115 N. Y. 437; Newby v. Colts, etc., Co., L. R. 7 Q. B. 293.

[7] Bawknight v. Liverpool, etc., Co., 55 Ga. 194; Ætna, etc., Co. v. Black, 80 Ind. 513; Parke v. Comw., etc., Co., 44 Pa. St. 422. The relation of attorney and client does not make the attorney a managing agent. Taylor v. Granite, etc., Assn., 136 N. Y. 343. The captain of a steamboat owned by a foreign corporation is not a managing agent. Upper Miss. Tr. Co. v.

§ 276. **Must be doing business in the state.**—According to the general rule, the service upon a foreign corporation can only be made upon an agent who is representing a corporation which is engaged in business in the state. The corporation must be in the state for the purpose of doing business, and it is not enough that the agent or representative of the corporation is simply within the limits of the state. "We are of the opinion," says Mr. Justice Field,[1] "that when service is made within the state upon the agent of a foreign corporation, it is essential, in order to support the jurisdiction of the court, to render a personal judgment that it should appear somewhere upon the record, either in the application for the writ, or accompanying its service, or in the pleadings or findings of the court, that the corporation was engaged in business in the state. The transaction of business by the corporation in the state, general or special, appearing, a certificate of service by the proper officer on a person who is its agent there would, in our opinion, be sufficient prima facie evidence that the agent represented the company in the business. It would then be open, when the record is offered in evidence in another state, to show that the agent stood in no representative character to the company, that his duties were limited to those of subordinate employe or to a particular transaction, or that his agency had ceased when the matter in suit arose."[2] The agents of a

Whittaker, 16 Wis. 220; a clerk in a store belonging to a foreign mining corporation is not a managing agent. Blanc v. Paymaster Min. Co., 95 Cal. 524. It has been held that an agent of a railway corporation who dealt only with its passenger business was not its general agent. Brewster v. Michigan C. R. Co., 5 How. Pr. 183. But later cases extend the rule. Thus, a general agent in the passenger department is a managing agent. Tuchband v. Chicago, etc., R. Co., 115 N. Y. 437. Service may be made upon a division superintendent in an action for injuries received on the division. Hills v. Richmond, etc., R. Co., 37 Fed. Rep. 660. See many cases digested in a *note* to 23 L. R. A. 496.

[1] St. Clair v. Cox, 106 U. S. 350.

[2] Freeman v. Alderson, 119 U. S. 185; Fitzgerald, etc., Co. v. Fitzgerald, 137 U. S. 98; Societe Foncier v. Millikin, 135 U. S. 304; Firemen's, etc., Co. v. Thompson, 155 Ill. 204; Blanc v. Paymaster, etc., Co., 95 Cal. 521; Moore v. Wayne Ct. Judge, 55 Mich. 84; Phillips v. Library Co., 141 Pa. St. 462; Camden, etc., Co. v. Swede, etc., Co., 32 N. J. L. 15; Midland, etc., R. Co. v. McDermid, 91 Ill. 170.

corporation are therefore not its agents for the purpose of service in a state where the corporation does not transact business.[1]

§ 277. **Service upon officer temporarily within the state.**— By the rule above stated a corporation which does not enter a foreign state for the purpose of doing business can not be subjected to the jurisdiction of the foreign state. "Statutory provisions for the service of process upon a foreign corporation must rest upon the fact of the foreign corporation doing business, or in some way exercising its corporate franchise, within the jurisdiction. A law which went beyond this would be beyond the power of any sovereign to enact."[2] Service can not be made upon an officer of a corporation who is in the state upon personal and not corporate business, and it has been held that this is true when he is temporarily there for the purpose of transacting a particular item of business for the corporation,[3] although the contrary rule prevails in New York. It is there held that "any service must be deemed sufficient which renders it reasonably probable that the party proceeded against will be apprised of what is going on against him, and have an opportunity to defend."[4]

In another case,[5] where the president of a corporation which

[1] State v. District Court, 26 Minn. 233; Phillips v. Library Co., 141 Pa. St. 462; Moulin v. Ins. Co., 24 N. J. L. 222; Newell v. Great, etc., R. Co., 19 Mich. 336. To constitute a person an agent of a foreign corporation upon whom service of a summons may be made he must be one actually appointed by and representing the corporation, and not one created by mere construction or implication contrary to the intention of the parties. Mikolas v. Hiram Walker & Sons (Minn.), 76 N. W. Rep. 36.

[2] Murfree For. Corp., § 208.

[3] Fitzgerald Const. Co. v. Fitzgerald, 137 U. S. 98; Good Hope Co. v. Railway, etc., Co., 22 Fed. Rep. 635. See also Golden v. Morning News, 42 Fed. Rep. 112, 156 U. S. 518; Latimer v. Railway Co., 43 Mo. 105; Camden etc., Co. v. Iron Co., 32 N. J. L. 15; St. Clair v. Cox, 106 U. S. 350. Service may be made on the president of a corporation who is in the state but not on official business if the cause of action arose in the state. Shickle, etc., Co. v. Wiley, etc., Co., 61 Mich. 226; Carsten v. Leidigh, etc., Co., 18 Wash. 450, 39 L. R. A. 548; Phillips v. Library, 141 Pa. St. 462; Rust v. United, etc., Co., 70 Fed. Rep. 129, 17 C. C. A. 16.

[4] Hiller v. Burlington, etc., R. Co., 70 N. Y. 223.

[5] Pope v. Terre Haute, etc., Co., 87 N. Y. 137; Gibbs v. Queen, etc., Co., 63 N. Y. 114.

had transacted no business in the state was served with a summons when passing through the state on his way to a summer resort, a judgment rendered on this service was held good for every purpose within the state. The court said: "The object of all service of process for the commencement of a suit, or any other legal proceeding, is to give notice to the party proceeded against, and any service which reasonably accomplishes that end answers the requirements of natural justice and fundamental law, and what service is to be deemed sufficient for that purpose is to be determined by the legislative power of the country in which the proceeding is instituted, subject only to the limitation that the service must be such as may reasonably be expected to give the notice aimed at."

Such service would certainly not be recognized in the courts of other states.[1]

In New York service on an officer or director who is temporarily in the state on his own business is good if the corporation has property in the state or the cause of action arose there.[2]

§ 278. **Illustrations.**—A certain firm in business in the state of Wisconsin filed their complaint in a Minnesota court against a Wisconsin corporation having no agent or place of business in Minnesota. The action was upon contracts made and to be executed in Wisconsin. A summons was issued and was served by the sheriff in Minnesota, by delivering a copy thereof to the president of the company, who was then within the state of Minnesota, not on any business of the company, but for his own personal business and pleasure, and who had no authority from the company to receive such service. The court said:[3] "The question sought to be raised in this proceeding is, can the courts of this state acquire jurisdiction over the person of a corporation created under the laws of another state, where the cause of action arose out of this state, and the corporation has no property

[1] Golden v. Morning News, 156 U. S. 518.

[2] Hiller v. Burlington, etc., R. Co., 70 N. Y. 223; Childs v. Harris, etc., Co., 104 N. Y. 477.

[3] State v. District Court, 26 Minn. 233; Latimer v. Railway Co., 43 Mo. 105, 97 Am. Dec. 378.

therein, and never transacted any business, nor had any office or agency, or officer, or agent therein, and the only ground for asserting such jurisdiction is that the summons was served within the state upon an officer of the corporation, who was in the state, not upon any business, nor by any authority of the corporation, but solely in a private capacity and for his own private business or pleasure? The relator first raised the question in the district court, by a motion, upon affidavits showing the facts, to set aside such a service of the summons, which motion being denied, it procured this writ of prohibition to issue. We have very little doubt that if the questions were properly before us for decision, we should sustain the objection to the jurisdiction. The facts in Guernsey v. American Ins. Co.[1] were sufficient to sustain the jurisdiction, but the reasoning of the court goes further than we can approve. But the writ of prohibition is not the proper remedy."

A statute which authorizes service upon an officer who is accidentally within the jurisdiction when the corporation does no business in the state is said to be so contrary to all ideas of justice that the courts of other states ought not to sanction it.[2] A provision for service on the officers of "any incorporated company" does not apply to a foreign corporation doing no business in the state, but whose officer is served while passing through the state.[3]

§ 279. **Statutory requirements.**—In all the states statutory methods are now provided for service of process upon foreign corporations which are doing business in the state. When a corporation complies with such provisions as to service and accepts them as a condition upon which it may do business in the state, the court acquires complete and perfect jurisdiction over it and may render a judgment *in personam* against it;[4]

[1] Guernsey v. American, etc., Co., 13 Minn. 278 (Gil. 256).

[2] Moulin v. Trenton, etc., Co., 24 N. J. L. 222.

[3] Midland, etc., R. Co. v. McDermid, 91 Ill. 170. See Shickle, etc., Co. v. Wiley, etc., Co., 61 Mich. 226. The language used in Hester v. Rasin, etc., Co., 33 S. C. 609, would seem to authorize service upon an officer of the corporation temporarily within the state when the cause of action arose elsewhere.

[4] Ex parte Schollenberger, 96 U. S.

and such a judgment is entitled to full faith and credit in other jurisdictions.[1] The statutes generally require the corporation to designate some one upon whom service may be made in the state.

"If a state permits a foreign corporation to do business within her limits, and at the same time provides that in suits against it for business there done process shall be served upon its agents, the provision is to be deemed a condition of the permission; and corporations that subsequently do business in the state are to be deemed to assent to such conditions as fully as though they had specially authorized their agents to receive service of the process."[2]

§ 280. **Designation of agent to accept service.**—Foreign corporations are sometimes required or permitted to name some state official as their agent to accept service of summons. Service on the insurance commissioner, who has been designated as prescribed by statute, is sufficient.[3] Such statutes apply only to companies doing business in the state.[4] The fact that the plaintiffs are the agents of the corporation does not deprive them of the statutory right to serve summons upon the state auditor.[5] When the statute authorizes service upon the secretary of state, service on the deputy of the secretary is defective.[6] But it is held that a superintendent of insurance may designate a clerk to accept service for him.[7] Service by mail is sufficient when there is a written admission of the re-

369; Wilson v. Martin-Wilson F. A. Co., 149 Mass. 24; Reyer v. Odd Fellows Assn., 157 Mass. 367; Benwood, etc., Works v. Hutchinson & Bro., 101 Pa. St. 359; Firemen's, etc., Co. v. Thompson, 155 Ill. 204.

[1] St. Clair v. Cox, 106 U. S. 350; Lafayette, etc., Co. v. French, 18 How. 404.

[2] St. Clair v. Cox, 106 U. S. 350; Gibbs v. Queen, etc., Co., 63 N. Y. 114, 20 Am. Rep. 513. There is no statute in Michigan providing for the service of process upon a foreign corporation where the cause of action did not accrue within the state. Grand Trunk R. Co. v. Wayne Circuit Judge, 106 Mich. 248.

[3] Osborne v. Shawmut, etc., Co., 51 Vt. 278.

[4] Hazeltine v. Mississippi Valley, etc., Co., 55 Fed. Rep. 743.

[5] Rehm v. German, etc., Co., 125 Ind. 135.

[6] Lonkey v. Keyes, etc., Co., 21 Nev. 312, 17 L. R. A. 351.

[7] South, etc., Co. v. Fire Assn. of Philadelphia, 67 Hun (N. Y.) 41.

ceipt of the summons.[1] A summons served on the insurance commissioner must be directed to him, but otherwise it must be in the usual form.[2] When a corporation has designated an agent as required by law, service thereafter upon a mere solicitor of the company is invalid.[3]

The agent so appointed need not be a person authorized to exercise any of the contractual powers of the corporation.[4] A certificate appointing the managing agent residing at a designated place is valid, although not naming the agent.[5] If a corporation fails to appoint an agent, as required, service may be made upon the agent in the state who transacted the business out of which the suit grew,[6] or upon any agent who can be found in the state.[7]

§ 281. **Service obtained by deception.**—On grounds of public policy it is held that service of a summons upon a defendant who has been induced to come within the jurisdiction of the

[1] Farmer v. National, etc., Assn., 50 Fed. Rep. 829. See, also, 67 Hun (N. Y.) 119.

[2] Westchester, etc., Co. v. Coverdale, 48 Kan. 446.

[3] Liblong v. Kansas, etc., Co., 82 Pa. St. 413; Thayer v. Tyler, 10 Gray (Mass.) 164.

[4] Nelms v. Edinburg, etc., Co., 92 Ala. 157.

[5] Goodwin v. Colo., etc., Co., 110 U. S. 1; Lafflin v. Travelers, etc., Co., 121 N. Y. 713.

[6] Funk v. Anglo-American, etc., Co., 27 Fed. Rep. 336.

[7] Hagerman v. Empire Slate Co., 97 Pa. St. 534. In Foster v. Charles Betcher, etc., Co. (S. Dak.), 23 L. R. A. 490, the court said: "The failure of the appellant to comply with the laws of the state can not be taken advantage of by itself, nor in fact by any private person in a collateral proceeding. The state only in its sovereign capacity can take advantage of such a failure of a foreign corporation to comply with the law. Wright v. Lee, 4 S. Dak. 237, 51 N. W. Rep. 706, 55 N. W. Rep. 931. If a foreign corporation is engaged in business in this state, though failing to comply with the law by filing a copy of its articles of incorporation and a certificate of the appointment of an agent, it is still subject to the laws of the state, and amenable to its process, until its right to so continue to do business within this state is declared forfeited by the courts of the state. The person transacting the business of the corporation in this state, as managing agent, must be presumed to be the agent of the corporation and subject to the service of process."

court for that purpose by the fraud of the plaintiff confers no jurisdiction.[1]

§ 282. **Proceedings by state against foreign corporation.**— A foreign corporation which is exercising its powers and franchises in a state without authority of law may be ousted therefrom by a proceeding in *quo warranto*.[2] Under certain circumstances the remedy may be by injunction.[3]

[1] Columbia, etc., Co. v. Bucyrus, etc., Co., 60 Minn. 142.

[2] In State v. Insurance Co., 49 Ohio 440, 31 N. E. Rep. 658, the court said: "It is claimed that, as the defendant is a foreign corporation, it can not be affected by a proceeding in *quo warranto* in the courts of the state. That it can not be ousted of the right to be a corporation or of any of the franchises conferred on it by the laws of New York is not doubted; but as to such franchises and privileges as are derived from the laws of the state of Ohio it is as much amenable to the courts of this state as an Ohio corporation, and, when found exercising such franchises without authority of law, it may be ousted therefrom." State v. Insurance Co., 47 Ohio St. 167; State v. Fidelity, etc., Co., 39 Minn. 538, 41 N. W. Rep. 108.

[3] Employers', etc., Corp. v. Employers', etc., Co., 16 N. Y. Supp. 397.

CHAPTER 12.

THE ACQUISITION AND LOSS OF MEMBERSHIP IN A CORPORATION.

§ 283. Non-stock corporations.
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§ 283. **Non-stock corporations.**—The method by which membership in a corporation without capital stock may be acquired must be determined from the charter or by-laws. If no restrictions are found in the charter, the admission of members is under the control of the corporation. Statutes authorizing and regulating the organization of such corporations always provide for the original membership and subsequent members are usually admitted upon an application and vote of approval by the existing members.[1]

§ 284. **Corporations having capital stock.**—Membership in a joint-stock corporation consists simply in the ownership of one or more shares of the stock.[2] The stock need not neces-

[1] State v. Sibley, 25 Minn. 387. In Am., etc., Co. v. Chicago, etc., Exch., 143 Ill. 210, the court, after referring to a rule or by-law regulating admission to membership in a non-stock corporation, said: "Said association had an undoubted right to adopt this rule, and as it prescribes the mode, and the only mode, in which membership in the exchange can be obtained, no one can justly claim to be a member who has not been admitted in the mode thus prescribed."

[2] State v. Ferris, 42 Conn. 560; Upton v. Hansbrough, 3 Biss. 417.

sarily have been paid for.[1] The possession of a stock certificate is not essential to membership, as it is merely evidence of the ownership of shares.[2] Nor does membership necessarily follow from the possession of the stock certificate alone, without participation in the business of the corporation.[3] But the party in whose name the stock appears on the books of the corporation is presumed to be the owner and a member, and the burden rests on him to show the contrary when it is attempted to hold him to the liabilities of membership.[4]

§ 285. **Who can be members.**—Every person who is capable of contracting is capable of becoming a member of a corporation. A corporation may be formed on terms which expressly exclude certain persons or classes of persons from becoming members of it,[5] but regulations to this effect do not affect the legal capacity of the persons excluded. Such capacity depends on the general law of the country, not on the regulations of any particular corporation. There is no general principle of law which prevents a corporation from holding stock in another corporation except the principle that a *corporation can not lawfully employ its funds for purposes not authorized by its charter.*[6]

§ 286. **Method of obtaining shares.**—The shares of a corporation may be acquired either by subscription before or after incorporation, or by acquiring them from one to whom they have already been issued and having them transferred on the books of the corporation. The mere fact of subscription does not make the subscriber a stockholder, as acceptance of the offer is necessary, but such acceptance will be presumed from

[1] Wheeler v. Millar, 90 N. Y. 353; Waukon, etc., R. Co. v. Dwyer, 49 Iowa 121; Downing v. Potts, 23 N. J. L. 66.

[2] Columbia, etc., Co. v. Dixon, 46 Minn. 463; Rutter v. Kilpatrick, 63 N. Y. 604; Hawley v. Upton, 102 U. S. 314.

[3] Baker v. Woolston, 27 Kan. 185.

[4] Holland v. Duluth, etc., Co., 65 Minn. 324; Barron v. Burrill, 86 Me. 72, 29 Atl. Rep. 938; Grindle v. Stone, 78 Me. 176; Turnbull v. Payson, 95 U. S. 418.

[5] Blieu v. Rand (Minn.), 79 N. W. Rep. 606.

[6] Lindley Law of Companies, 36, 43; Pearson v. Concord R. Co., 62 N. H. 537, Wilgus' Cases.

very slight circumstances.[1] Hence, membership in the corporation dates from the time the offer contained in the subscription is accepted.[2] The actual taking of shares of stock is equivalent to subscription for and an agreement to take them.[3] A completed transfer of shares transfers the membership in the corporation.[4] The books of the corporation are the primary evidence of membership,[5] and until a transfer is made on the corporate books the party there registered remains a member, although he may have pledged the stock certificates,[6] or authorized their transfer on the books of the company.[7]

[1] Barron v. Burrill, 86 Maine 72, 29 Atl. Rep. 938.

[2] McClure v. People's, etc., Co., 90 Pa. St. 269; Busey v. Hooper, 35 Md. 15.

[3] Barron v. Burrill, 82 Me. 72.

[4] Supply, etc., Co. v. Elliott, 10 Colo. 327; Hawkins v. Glenn, 131 U. S. 319.

[5] In re St. Lawrence, etc., Co., 44 N. J. L. 529.

[6] Vail v. Hamilton, 85 N. Y. 453; Merchants' Bank v. Cook, 4 Pick. 405; Hoppin v. Buffum, 9 R. I. 513; McDaniels v. Flower, etc., Co., 22 Vt. 274.

[7] McNeil v. Tenth Nat'l Bank, 46 N. Y. 325, Wilgus' Cases.

In Bissell v. Heath, 98 Mich. 472, 57 N. W. Rep. 585, the court said: "It is claimed by appellant that he was not a stockholder. It appears by the record that, about the time the bank was organized, the defendant negotiated with one Solon H. Wilhelm, who became cashier of the bank, for the purchase of stock. It appears by the stock ledger that under date of January 3, 1887, there was issued to defendant a certificate of stock, the stock ledger stating that the stock was transferred from subscriptions of S. S. W. It further appears that a certificate was in fact issued to the defendant, and that he received dividends for several years. It is urged that the only way in which the defendant, not being an original subscriber to the capital stock, could become a stockholder, was by securing a transfer of some of the stock subscribed for by others, and that no formal transfer appears upon the bank books, and hence that he never legally become a stockholder. The answer to this is, that the evidence of the transfer was sufficient to satisfy the corporators. The stock was, in fact, issued and the books of the company showed it sufficiently. Bank v. Warren, 52 Mich. 557, 18 N. W. Rep. 356. The corporation was bound by the issue of stock. It could waive the formality of any assignment by S. S. W., and, having done so, could not thereafter deny defendant's rights on the ground that he had failed to produce evidence of an assignment from an original subscriber to the capital stock."

A corporation may waive formalities prescribed by its charter or by-laws in making an original subscription or a transfer of shares. And if a person has been received as a shareholder, and has acted as shareholder, and enjoyed the privileges of a shareholder he will be estopped from denying that he agreed to become a shareholder and to assume the inci-

§ 287. **Effect of delivery of stock certificate.**—Where the stock of a corporation is by the terms of the charter or by-law transferable only on its books, the purchaser who receives a certificate, with power of attorney, gets the entire title, legal and equitable, as between himself and his seller, with all the rights the latter possessed.[1] But as between himself and the corporation he acquires only an equitable title, which they are bound to recognize and permit to ripen into a legal title when he presents himself, before any effective transfer on the books has been made and offers to do the acts required by the charter or by-laws in order to make a transfer. Until those acts be done he is not a stockholder, and has no claim to act as such,[2] but possesses, as between himself and the corporation, by virtue of the certificate and power, the right to make himself, or whomsoever he chooses, a stockholder by the prescribed transfer. The stock not having passed by the delivery of the certificate and power of attorney, the legal title remains in the seller, so far as affects the company and subsequent bona fide purchasers, who take by transfer duly made on the books. And hence a buyer, in good faith, from the person in whose name the stock stands on the books, who takes a transfer in the manner provided in the by-laws, becomes vested with a complete title to the stock, which cuts off all the rights and equities of the holder of the certificate. What other rights and equities he may possess is another question; but if the transferee has taken in good faith, and for value, the stock is beyond his reach, and beyond recall by the corporation.[3]

§ 288. **Compliance with conditions.**—A person can not, properly speaking, be said to be a member of or shareholder in a corporation so long as he has only a right to become such; nor can a person who has become a member or a shareholder

dental liabilities both to the company and its creditors. Morawetz, II, § 841.

[1] See Ch. 16.

[2] "A transfer not entered on the books of the company has no validity outside of the parties to such transfer." People v. Robinson, 64 Cal. 373.

[3] New York & N. H. R. Co. v. Schuyler, 34 N. Y. 30, per Davis, J.; Stebbins v. Insurance Co., 3 Paige 350; Bank v. Laird, 2 Wheat. 390; Bargate v. Shortridge, 5 H. L. Cas. 297.

be properly said to have ceased to be one so long as he has only a right to retire. If a person who is not a shareholder omits to do what is necessary to render himself a shareholder, he remains a non-shareholder, although very little may be wanting to render him a shareholder. On the other hand, if a person, who is a shareholder already, omits to do what is necessary to retire, he continues to be a shareholder whatever intention he may have had of withdrawing from the company, and whatever preliminary steps he may have taken for that purpose. In these cases, that which is necessary to change an existing state of things has not happened; the right to enter or leave the company has not been exercised; and until such right has been exercised, membership, in the proper sense of the word, has not been created in the one case, and has not ceased in the other.[1]

§ 289. **Estoppel to deny membership.**[2]—A person may sometimes be treated as a member, although he has not complied with the necessary preliminary conditions. The performance of certain conditions and the observance of formalities may sometimes be waived and irregular acts may be confirmed. Hence if, notwithstanding the failure to comply with conditions, or the existence of irregularities in the issue of the shares, the party has been treated as a shareholder by the corporation, and has acted as a stockholder, both he and the corporation will be estopped to deny the relation. So, if a shareholder, who has a right to retire, has in fact retired and been treated by the corporation as if he was no longer a member, both he and the company will be estopped to deny that he has ceased to be a member, although he may not have retired regularly and properly.[3] The corporation will not be

[1] Lindley Law of Companies, 44. "The type then of a member of a company," says this learned writer, "is a person who has agreed to become a member, and with respect to whom all conditions precedent to the acquisition of the rights of a member have been duly observed. Where all these circumstances are combined, there is membership in the fullest and most accurate sense."

[2] McCarthy v. La Vasche, 89 Ill. 270, Wilgus' Cases.

[3] Lindley Law of Companies, 48; Jewell v. Rock River, etc., Co., 101 Ill. 57; Union, etc., Assn. v. Selig-

permitted to take advantage of the non-observance of formalities which it has tacitly waived, and a person who has acted as and received the benefits of membership will not be heard to say that he has neglected to comply with certain formalities or conditions when called upon to assume the burdens incident to membership.[1] Thus, where it did not appear that the defendant had ever had a certificate of stock in his possession, but did appear that he authorized a share to be issued to him, that a certificate had actually been issued, that only stockholders are eligible to office, that he was upon the organization of the company elected its president and served for a long time in that capacity, and that he had paid a number of installments upon a share of stock, it was held sufficient to charge him as a member and that he was estopped to deny his subscription.[2] The right to membership in a corporation was restricted to persons of a certain nationality, and the defendants subscribed and paid for stock, and accepted certificates therefor, and appeared as stockholders on the books of the corporation for a period of three years, during which time debts were contracted and the corporation became insolvent. In an action to enforce the statutory liability for the benefit of creditors they were held to be estopped to assert that they were not stockholders because they were not of the required nationality.[3]

§ 290. **The holder of illegally issued shares.**—There can be no membership acquired through the holding of shares of

man, 92 Mo. 635; Griswold v. Seligman, 72 Mo. 110; Bissell v. Heath (Mich., 1894), 57 N. W. Rep. 585; York Park, etc., Assn. v. Barnes (Neb., 1894), 58 N. W. Rep. 440; Sanger v. Upton, 91 U. S. 56; Musgrave v. Morrison, 54 Md. 161; Boston, etc., R. Co. v. Wellington, 113 Mass. 79; Chaffin v. Cummings, 37 Me. 76.

[1] Barnes v. Pennell, 2 H. L. C. 496; Cheltenham, etc., R. Co. v. Daniel, 2 Q. B. Ad. & E. 281, 42 Eng. C. L. 675; Sheffield, etc., Co. v. Woodcock, 7 M. & W. 574; Cromford, etc., R. Co. v. Lacey, 3 Y. & J. 79; Murray v. Bush, L. R. 6 H. L. 37, and cases cited in preceding note.

[2] York Park, etc., Assn. v. Barnes (Neb., 1894), 58 N. W. Rep. 440; Sanger v. Upton, 91 U. S. 56. One who subscribes for stock in a corporation, acts as an officer thereof, and takes part in its management can not dispute the validity of the corporation. Warehousing Co. v. Badger, 67 N. Y. 294.

[3] Blien v. Rand (Minn., June 22, 1899), 79 N. W. Rep. 606.

stock which under no circumstances could legally exist,[1] but if the corporation had power to issue the shares, the corporation and the holder of the shares may be estopped from denying their existence, although they were issued irregularly and improperly.[2]

§ 291. **Disfranchisement — Joint stock companies.**—Membership in a joint stock corporation consists in the ownership of its stock, and is therefore lost by a transfer of the stock in due form. Although the title to corporate property is in the corporation and not in the stockholder, the latter has what may be called the ultimate ownership, and of this he can not be deprived by any act of the corporation. It follows that the power to disfranchise or expel a member of such a corporation never exists unless expressly conferred by the charter.[3] The same rule is held to apply to every corporation or society formed primarily or exclusively for gain,[4] or which holds property.[5]

§ 292. **Disfranchisement in non-stock corporations.**—A non-stock corporation, not organized exclusively for the purpose of gain, has implied power, unless restrained by its charter, to expel a member for cause.[6] In England it is held that in the absence of a grant an incorporated voluntary association has no inherent power to expel a member.[7] The questions commonly arise in connection with social clubs and such organi-

[1] Bank of Hindustan v. Alison, L. R. 6 C. P. 54.

[2] Campbell's Case, 9 Ch. App. Cases 1. In Nenney v. Waddill (Tex., 1894), 25 S. W. Rep. 308, it was held that the constitutional provision forbidding the issue of stock except for value received, and avoiding all fictitious issues of stock, can not be invoked by stockholders who have knowingly accepted "paid up" stock to twice the amount of their subscriptions.

[3] Edgerton Tobacco, etc., Co. v. Croft, 69 Wis. 256, 34 N. W. Rep. 143; In re Long Island R. Co., 19 Wend. 37, 32 Am. Dec. 429, Wilgus' Cases.

[4] In re Long Island R. Co., 19 Wend. 37, 32 Am. Dec. 429; Evans v. Philadelphia Club, 50 Pa. St. 107, Wilgus' Cases.

[5] Bagg's Case, 11 Co. 93. See note to Hiss v. Bartlett, 3 Gray 468, in 63 Am. Dec. 772.

[6] As to expulsion of members of a subordinate lodge of a beneficial order, see opinion of Judge Thompson, Mulroy v. Supreme Lodge, etc., 28 Mo. App. 463.

[7] Dawkins v. Antrobus, L. R. 17 Ch.

zations as boards of trade and chambers of commerce. The power to expel a member is usually conferred in general language by the charter, and the particular grounds of expulsion and procedure is provided for in the by-laws or rules of the corporation. In the leading English case,[1] decided before joint-stock business corporations became common, Lord Mansfield said that there were three sorts of offenses for which an officer or corporator might be expelled: (1) Such as have no immediate relation to his office, but are in themselves of so infamous a nature as to render the offender unfit to execute any public franchise. (2) Such as are only against the oath and the duty of his office as a corporator, and amount to a breach of a tacit condition annexed to his franchise or office. (3) The third sort of offense for which an officer or corporator may be displaced is of a mixed nature, as being not only against the duties of his office, but also a matter indictable at common law. For the first sort of offenses there must be a previous conviction upon an indictment. When the offense is merely against his duty as a corporator he can only be tried for it by the corporation. Generally the offense must be of an infamous character, and have some relation to the duties which attach to membership in the corporation. "When a corporation is duly organized it has power to make by-laws and expel members, though the charter is silent upon the subject. If the power is expressly granted in general terms, it is conferred to enable the corporation to accomplish the objects of its creation, and is limited to such objects or purposes. It appears to be well settled that when the charter of a corporation is silent upon the subject of expulsion, or grants the power in general terms, there are but three legal causes of disfranchisement: 1. Offenses of an infamous character, indictable at common

Div. 615, 44 Law T. Rep. (N. S.) 557.

[1] Rex v. Richardson, 1 Burr. 517. See review of English cases in Richards v. Clarksburg, 30 W. Va. 491; Comw. v. St. Patrick's, etc., 2 Binn. (Pa.) 441, 4 Am. Dec. 453; People v. Medical, etc., 32 N. Y. 187. Notes to Hiss v. Bartlett, 63 Am. Dec. 772; Austin v. Searing, 69 Am. Dec. 665; Society v. Comw., 52 Pa. St. 125, 91 Am. Dec. 139.

law. 2. Offenses against the corporator's duty to the corporation as a member of it. 3. Offenses compounded of the two."[1]

§ 293. **Nature of membership in non-stock corporations.**— Membership in certain non-stock corporations, such as boards of trade and chambers of commerce, is valuable property which may be sold and transferred subject to the restrictions imposed by the rules and by-laws of the corporation. But it is property in a restricted sense only, and is always held incumbered by the conditions, without which it could not have been obtained.[2] In a recent New York case[3] it is said: "When membership and the rights belonging to that status were conferred upon him the gift was accompanied by the condition that the rights of whatever nature should revert to the association upon the happening of certain events; and he can not be heard to complain, nor can third persons claiming to derive under him. He should be held to a contract which was reasonable when entered into, which prejudiced no rights of persons and were in conflict with no statutory or common law right. A person acquires by membership in the association only such rights as the constitution and by-laws give him." Hence, the corporation may provide that membership can not be transferred without the consent of the other members or until all contracts entered into with the other members are fulfilled.[4]

[1] State v. Chamber, etc., 20 Wis. 68.

[2] Hyde v. Ward, 94 U. S. 23; In re Haebler, 149 N. Y. 414, 44 N. E. Rep. 87.

[3] Belton v. Hatch, 109 N. Y. 593, 17 N. E. Rep. 225. The rule is that members are bound by the by-laws of the corporation. See Green v. Board of Trade (Ill.), 51 N. E. Rep. 99; In re Haebler, 149 N. Y. 414, 44 N. E. Rep. 87, the court said: "The relator had a right to become a member of this corporation and to agree to be governed by its charter and by-laws; and they express the contract by which he and every other member is bound, and which measures their rights, duties and liabilities as members. Weston v. Ives, 97 N. Y. 222; Belton v. Hatch, 109 N. Y. 593; O'Brien v. Grant, 146 N. Y. 163. A member of a corporation may so hedge himself in by agreement as to yield the protection which one seeks in the ordinary affairs of life, and to enlarge the authority that may be used against him. People v. New York, etc., Exchange, 8 Hun 216, 220."

[4] American, etc., Com. Co. v. Chicago, etc., Exchange, 143 Ill. 210; Board of Trade, etc., v. Nelson, 162 Ill. 431, 53 Am. S. R. 312.

§ 294. **Grounds for expulsion.**—When authority is conferred to expel a member for reasonable cause or for a designated offense, the corporation has the right, through its proper officers or body, to determine the sufficiency of the cause and what constitutes the offense,[1] subject to the power of the courts to restrain arbitrary and illegal action.[2] A member of a society may be expelled for conduct calculated to bring the society into disrepute.[3] Under a by-law which makes "slander against the society" an offense, it was held that a member could be expelled, but there must be a written charge entered upon the books of the corporation.[4] One member of a corporation can not be expelled for villifying another member, as such an offense is said not to affect the interest or good government of the corporation or be indictable at common law.[5] An incorporated board of trade may suspend a member under a by-law which provides that "when a member shall be guilty of any act of bad faith or any attempt at extortion, or any other dishonorable or dishonest conduct, he shall be censured, suspended or expelled by the board of directors as they may determine."[6] A mere breach of contract without moral delinquency on the part of a member is not within a by-law authorizing the board of managers to expel a member for "fraudulent breach of contract, or any proceeding inconsistent with

[1] Inderwick v. Snell, 2 Mac. & G. 216; B. & S. Smith Society v. Vandyke, 2 Whart. (Pa.) 309, 30 Am. Dec. 263.

[2] People v. Higgins, 15 Ill. 110.

[3] Burton v. St. George Society, 28 Mich. 261.

[4] Rohler v. Mechanics Aid Society, 22 Mich. 86. The offense must, however, be analogous to the common law offense of slander.

[5] Comm. v. St. Patrick Ben. Assn., 2 Binn. (Pa.) 441.

[6] Board of Trade v. Nelson, 162 Ill. 431, 44 N. E. Rep. 743. Expulsion may be for non-performance of the contract: White v. Brownell, 2 Daly's Rep. (N. Y.) 329. Insolvency; Slander of the society and its members: People v. Mechanics' Aid Society, 22 Mich. 86. Publication of a libelous pamphlet on another member: Dawkins v. Antrobus, L. R. 17 Ch. Div. 615. But see Beesley v. Chicago, etc., Assn., 44 Ill. App. 278. Moral delinquency: People v. St. Stephen's Church, 53 N. Y. 103. The following are insufficient to justify expulsion: "Unprofessional conduct in advertising": People v. Med. Soc., 32 N. Y. 187. "Doing business at less than the established tariff of the society": People v. Med. Soc., 24 Barb. (N. Y.) 570. As to whether a member of a club can be expelled for striking another member, see Evans v. Phila. Club, 50 Pa. St. 107.

just and equitable principles of trade."[1] The charter stated that the object of a corporation was "to inculcate just and equitable principles of trade, to establish and maintain uniform and commercial usages * * * and to adjust misunderstandings between persons engaged in business:" A member of a produce exchange may be expelled for unjustifiable breach of a contract not made on the floor of the exchange,[2] or for obtaining goods from one not a member under false pretenses.[3] But a by-law made under general authority must be reasonable,[4] and it has been held that there can not be expulsion for violation of an unenforcible by-law when the offense is in no way injurious to the corporation.[5]

§ 295. **The proceedings.**—The proceedings for the expulsion of a member of a non-stock corporation may be provided for by the by-laws.[6] In such cases they must be strictly observed or the conviction can not be sustained.[7] Generally

[1] People v. N. Y. Produce Exchange, 149 N. Y. 401.

[2] In re Haebler, 149 N. Y. 414, 44 N. E. Rep. 87. As to jurisdiction of stock exchange arbitration committee, see Cochran v. Phila. Stock Exch., 180 Pa. St. 289.

[3] People v. N. Y. Com. Assn., 18 Abb. Pr. 271.

[4] Hibernia Ins. Co. v. Comw., 19 Pa. St. 267. A by-law limiting the number of solicitors that a member of a stock exchange may employ with penalty of expulsion is illegal, because in restraint of trade. People v. Chicago Live Stock Ex., 170 Ill. 556, 39 L. R. A. 373.

[5] Evans v. Phil. Club, 50 Pa. St. 107. See cases collected in note to 63 Am. Dec. 772.

[6] State v. Trustees, 5 Ind. 77; Comw. v. German Society, 15 Pa. St. 251. A rule that when any member commits a grave offense or act of dishonesty involving the association, a committee shall be appointed to make a preliminary investigation, is reasonable and a member has no right to notice of such preliminary investigation.

[7] Fisher v. Keane, L. R. 11 Ch. Div. 353; Greene v. Board, etc. (Ill.), 51 N. E. Rep. 599; Commonwealth v. Union League, 135 Pa. St. 301, 19 Atl. Rep. 1030, is an elaborate consideration of the powers of a social club to expel members for acts which are deemed prejudicial to the organization. It was held that where the trial was conducted in due form and in good faith by the club, the courts would not inquire into the question of guilt. The only question in the case as stated by the court was one of power. The case was distinguished from Evans v. Philadelphia Club, 50 Pa.St.107, on the ground that in that case there was no express power of expulsion conferred by the charter and the case rested upon the ground that the offense was not such as to fall within the inherent powers of the corporation at common law. It was said that the common law power of expulsion as declared in that case may be thus stated.

there must be a provision for a hearing with an opportunity to offer testimony and examine witnesses, although it has been held that on a hearing before a committee of the membership of a board of trade the accused is not entitled to professional counsel.[1] If there is no provision to the contrary the power of disfranchisement rests in the whole body of membership,[2] but it may be conferred upon the board of directors by a by-law regularly passed by the members.[3] In corporations such as social clubs and boards of trade it may be exercised by a body provided for by the charter or the by-laws. But as said in one case: "The transfer from the body of the society where it properly belongs, to a small fraction of its members of so large and dangerous a power as that of expulsion, must appear, if it be claimed to exist, by the plainest language. It can not be established by inference, or presumption, for no such presumption is to be made in derogation of the right of the whole body, nor is it to be supposed, unless it appears by the most express and unambiguous language, that the members of the society have consented to hold their rights and membership by

"First, the power of disfranchisement must in general be conferred by the charter. It is not sustained as an incidental power, excepting (1) when the member has been legally convicted of an infamous offense, and (2) when he has committed some act tending to the destruction or injury of the society. Second, the power to make by-laws is incidental to corporations, but is generally conferred by charter. By-laws, however, which vest in a majority the power of expulsion, for minor offenses, are void, and expulsion under them will not be sustained. Third, in joint stock companies or corporations owning property, no power of expulsion can be exercised unless conferred by statute."

[1] Greene v. Board, etc. (Ill.), 51 N. E. Rep. 599; Hassler v. Philadelphia, etc., 14 Phila. 233.

[2] State v. Chamber of Commerce, 20 Wis. 68; Medical and Surgical Society v. Weatherly, 75 Ala. 248; Gray v. Christian, etc., Soc., 137 Mass. 329, 50 Am. Rep. 310; Commonwealth v. Union League Club, 135 Pa. St. 301.

[3] State v. Chamber of Commerce, 47 Wis. 670. "Expulsion by the action of the directors is one mode or manner of expulsion; expulsion by a majority vote of all the corporators is another mode or manner of expulsion. A rule prescribing the former mode is as much authorized and justified by the language of the charter as a rule prescribing the latter mode." The charter provided that the corporation "shall have the right to admit or expel such members as they may see fit, in the manner to be prescribed by the rules, regulations and by-laws thereof." Pitcher v. Board, etc., 121 Ill. 412.

so frail a tenure as the judgment of a small portion of their own number.''[1]

§ 296. **Notice.**—It is necessary to the validity of the suspension or expulsion of a member of an incorporated society, that the accused should be notified of the charge against him and of the time and place set for the hearing; that the accusing body should proceed upon inquiry and consequently upon evidence, and that the accused should have a fair opportunity of being heard in his defense.[2] Notice is not rendered unnecessary by an express grant of power to expel.[3] A by-law which authorized expulsion without notice is void.[4] When property rights are involved and no other method is provided by the by-laws notice must be personal,[5] and merely posting a notice in the club house is not sufficient.[6] Lack of notice is waived by a general appearance,[7] but not by an appearance and objection to proceeding without the presence of the prosecutor.[8] Service of a notice is not excused by the insanity of the member.[9] The notice must contain a statement of the

[1] Hassler v. Philadelphia, etc., 14 Phila. 233. As to power to revise a membership list of a lodge and drop members for non-payment of assessments, see Knights of Honor v. Mickser, 72 Texas 257; Medical and Surgical Society v. Weatherly, 75 Ala. 248.

[2] Thomp. Corp., § 881; People v. New York Com. Assn., 18 Abb. Pr. 271; Bagg's Case, 11 Co. 93; Fisher v. Keane, L. R. 11 Ch. Div. 353; Wachtel v. Society, 84 N. Y. 28; Diligent, etc., Co. v. Comm., 75 Pa. St. 291. The corporation acts in a *quasi* judicial capacity. See Otto v. Union, 75 Cal. 308; Burt v. Lodge, 66 Mich. 85, 33 N. W. Rep. 13.

[3] DeLacy v. Neuse Riv., etc., Co., 1 Hawks 274, 9 Am. Dec. 636.

[4] Erd v. Bavarian, etc., Assn., 67 Mich. 233. But it has been held that, when no property rights are involved and the by-laws do not provide for notice, no notice is necessary. Manning v. San Antonio Club, 63 Tex. 166, 51 Am. Rep. 639.

[5] Wachtel v. Society, 84 N. Y. 28; People v. Med. Soc., 32 N. Y. 187. Service of notice is not excused by a change of residence. Wachtel v. Society, 84 N. Y. 28.

[6] Sibley v. Carteret Club, 40 N. J. L. 295.

[7] Comm. v. Pennsylvania, etc., Soc., 2 Serg. & Rawl. 141; Sperry's App., 116 Pa. St. 391; Burton v. St. George Soc., 28 Mich. 261.

[8] People v. Mus., etc., Union, 101 N. Y. 680. It has been held that notice is not waived by appearing and entering upon the defense. Downing v. St. Columba's, etc., Soc., 10 Daly (N. Y.) 262; Labouchere v. Earl, etc., L. R. 13 Ch. Div. 346.

[9] Supreme Lodge v. Zuhlke, 129 Ill. 298.

charge[1] and the trial be fair and open[2] before an unprejudiced body.[3] This does not, however, require the impartiality of a judicial tribunal, and it has been held that it is no objection that one of the trial body was related to one of the parties, and that the proceedings are not affected by the fact that two members thereof were prejudiced.[4] "The principle to be deduced from all these cases is, that in every proceeding before a club, society or association having for its object the expulsion of a member, the member is entitled to be fully and fairly informed of the charge and to be fully and fairly heard."[5] This rule requiring notice and a hearing does not apply to mutual benefit corporations whose charters provide that non-payment of assessments after notice shall *ipso facto* work a forfeiture of membership.[6] In such cases the right to notice has been waived or parted with by contract.[7] But when there is no rule providing for such a forfeiture, there must be an adjudication of forfeiture by the corporation after notice to the member and a hearing upon the issue.

§ 297. **Incorporated and unincorporated societies.**—In some of the decisions no distinction is made between incorporated and unincorporated societies. In speaking of an unincorporated voluntary association, the supreme court of Pennsylvania[8] said: "These associations have some elements in common with corporations, joint-stock companies and partnerships; such as association and being governed by regulations adopted by themselves for that purpose. * * * I have very little doubt, therefore, that the same rules of law and equity, so far as regards the control of them and the adjudication of their reserved and inherent powers to regulate the conduct and to ex-

[1] Murdock's Case, 7 Pick. (Mass.) 303; Sleeper v. Franklyn Lyceum, 7 R. I. 523.

[2] State v. Adams, 44 Mo. 570.

[3] Smith v. Nelson, 18 Vt. 511.

[4] Loubat v. LeRoy, 15 Abb. N. C. 1.

[5] Hutchinson v. Lawrence, 67 How. Pr. 38.

[6] Thom. Priv. Corp., §§ 881, 898. See Schentler v. Grand Lodge, 45 Minn. 256.

[7] Blisset v. Daniel, 10 Hare 478.

[8] Leech v. Harris, 2 Brewst. 571.

pel their members, apply to them as to corporations and joint-stock companies."[1]

Greater power with reference to making rules for the government of members is sometimes recognized as belonging to unincorporated associations, and they are placed under no restrictions, so long as they do not conflict with general laws.[2]

§ 298. **Review by the courts.**—The power of expulsion is vested in the corporation, and when it is exercised by the proper body in good faith the court will not review the proceedings.[3] Where there has been a trial after due notice, and a conviction, the proceedings will not be inquired into collaterally.[4] In a case where the plaintiff had been expelled from a benevolent society, Chief Justice Gibson said:[5] "Into the regularity of these proceedings it is not permitted us to look. The sentence of the society, acting in a judicial capacity, and with undoubted jurisdiction of the subject-matter, is not to be questioned collaterally while it remains unreviewed by superior authority. If the plaintiff has been expelled irregularly, he has his remedy by mandamus to restore him, but neither by mandamus nor action can the merits of the expulsion be re-examined."[6] Under this rule the courts will investigate the proceedings in order to determine whether they are regular,

[1] Gormon v. Russell, 14 Cal. 532; Babb v. Reed, 5 Rawle's Rep. 151, 28 Am. Dec. 650; Otto v. Union, 75 Cal. 308; People v. Board of Trade, 80 Ill. 137; Anacosta Tribe v. Murbach, 13 Md. 91.

[2] White v. Brownell, 2 Daly 329; State v. Williams, 75 N. C. 134; Dawkins v. Antrobus, L. R. 17 Ch. Div. 615; Labouchere v. Earl of Wharncliffe, L. R. 13 Ch. Div. 346.

[3] Illinois, etc., Soc. v. Baldwin, 86 Ill. 479; Olmstead v. Farmer, etc., Co., 50 Mich. 200. In the celebrated Bently case, 2 Lord Raymond 1334, Mr. Justice Fortescue says: "The laws of God and man both give a party an opportunity to make defense if he has any. I remember to have heard it observed by a very learned man upon such an action that even God himself did not pass sentence upon Adam before he was called on to make his defense. Adam, says God, where art thou? Hast thou not eaten of the tree whereof I commanded thee that thou shouldst not eat? And the same question was put to Eve also."

[4] Otto v. Union, 75 Cal. 308.

[5] Black, etc., Society v. Vandyke, 2 Whart. 309.

[6] Lewis v. Wilson, 121 N. Y. 284, 24 N. E. Rep. 474; People v. N. Y., etc., Exch., 149 N. Y. 401.

and whether the cause is one for which, under the charter, there can be a legal expulsion, or whether the act complained of comes within the by-laws.[1] Subject to these limitations the corporations are left to enforce their own rules with reference to expulsion, and generally the courts will interfere only when a clear case of injustice is made out.[2] The remedy for wrongful expulsion is generally mandamus to compel reinstatement,[3] and not by injunction,[4] although this remedy is permitted in some cases.[5] The right of a member to be reinstated may be lost through his laches.[6]

[1] Labouchere v. Earl of Wharncliffe, L. R. 13 Ch. Div. 346; People v. Board of Trade, 80 Ill. 137.

[2] State v. Georgia Med. Soc., 33 Ga. 608.

[3] Evans v. Phila. Club, 50 Pa. St. 107; State v. Cham. of Com., 47 Wis. 670; Otto v. Union, 75 Cal. 308; Sibley v. Carteret Club, 40 N. J. L. 295; Notes to Dane v. Derby, 89 Am. Dec. 736, and Society v. Commonwealth, 91 Am. Dec. 139.

[4] Gregg v. Mass. Med. Soc., 111 Mass. 185; Sturges v. Board of Trade, 86 Ill. 441.

[5] Olery v. Brown, 51 How. Pr. (N. Y.) 92.

[6] Meherin v. San Francisco, etc., Exch., 117 Cal. 215.

CHAPTER 13.

CAPITAL STOCK.

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§ 299. **Capital.**—The capital of a corporation is the fund with which it transacts its business, and embraces all its property, real and personal. It is the property or means contributed

by the stockholders as the fund or basis for the business enterprise, for which the corporation was formed.[1] It signifies "the actual estate, whether in money or property, which is owned by an individual or a corporation. In reference to a corporation, it is the aggregate of the sum subscribed and paid in, or secured to be paid in, by the shareholders, with the addition of all gains or profits realized in the use and investment of those sums, or, if losses have been incurred, then it is the residue after deducting such losses."[2]

§ 300. **Capital stock.**—There is a distinction between the capital and the capital stock of a corporation, although the terms are often used interchangeably.[3]

The word capital when properly used refers to the property of the corporation while the capital stock represents the in-

[1] Iron R. Co. v. Lawrence, etc., Co, 49 Ohio St. 102, 30 N. E. Rep. 616.

[2] People v. Commissioners, 23 N. Y. 192 on 219; Bailey v. Clark, 21 Wall. 284; Christensen v. Eno, 106 N. Y. 97.

[3] San Francisco v. Spring Valley Water Works, 63 Cal. 529; Christensen v. Eno, 106 N. Y. 97. In Williams v. Western Union, etc., Co., 93 N. Y. 162, in considering a statute which provided that the directors should not withdraw or in any way pay to the stockholders any part of the capital stock of the corporation, or reduce the capital stock without the assent of the legislature, the court said: "The 'capital stock' in this section does not mean shares of stock, but it means the property of the corporation contributed by its stockholders or otherwise obtained by it to the extent required by its charter. While the term 'capital stock' is frequently used in a loose and indefinite sense, in this section and in legal phrase generally it means that and nothing more. In State v. Morristown, etc., Assn., 23 N. J. L. 195, Green, C. J., said: The phrase 'capital stock' is generally, if not universally, used to designate the amount of capital to be contributed for the purposes of the corporation. The amount thus contributed constitutes the capital stock of the company." In Burrall v. Railroad Co., 75 N. Y. 211, Folger, J., defined "capital stock" as that money or property which is put in a single corporate fund by those who by subscription therefor become members of a corporate body. See to same effect Barry v. Exchange Co., 1 Sandf. Ch. (N. Y.) 280. "The capital stock is to be clearly distinguished from the amount of property possessed by the corporation. Occasionally it happens that under the terms of statutes relating to stock, which have been drawn without regard to the technical meaning of words, the court will construe the capital stock to mean all the actual property of a corporation." Cook 1, § 9, citing Ohio R. Co. v. Weber, 96 Ill. 443; Philadelphia v. Ridge Avenue R. Co., 102 Pa. St. 190; Security Co. v. Hartford, 61 Conn. 89, 23 Atl. Rep. 699.

terest of the stockholders in the corporation. The amount of the capital stock is determined by the charter and remains fixed except as increased or decreased in the manner provided by law, while the amount of capital which a corporation may acquire is limited only by its success in acquisition and accumulation.[1] The value of the capital stock is measured by the value of the corporate property.[2] The capital stock determines the amount of the capital which must be kept unimpaired for the benefit of creditors while the corporation exists. Whatever is acquired in excess of this is surplus and may be distributed as profits, but until divided such surplus belongs to the corporation, and in a general sense may be regarded as a portion of its capital.[3]

§ 301. **Shares of stock.**—A share of stock is an incorporeal, intangible thing.[4] It is a right to a certain proportion of the capital stock of the corporation—never realized except upon the dissolution and winding up of the corporation—with the right to receive in the meantime such profits as may be made in the shape of dividends.[5] In other words, it is the "right to partake according to the amount put into the fund in the surplus profits of the corporation, and ultimately on the dissolution of it in the assets remaining after the payment of its debts."[6]

"The expression, shares of stock, when qualified by words indicating number and ownership, expresses the extent of the owner's interest in the corporation property. The interest is

[1] Farrington v. Tennessee, 95 U. S. 686; Wetherbee v. Baker, 35 N. J. Eq. 501; People v. Coleman, 126 N. Y. 433, Wilgus' Cases.

[2] Raleigh, etc., R. Co. v. Wake, 87 N. C. 414.

[3] Williams v. Western Union, etc., Co., 93 N. Y. 162; Farrington v. Tennessee, 95 U. S. 689; Phelps v. Farmers' Bank, 26 Conn. 279.

[4] Jermain v. Lake Shore, etc., R. Co., 91 N. Y. 483; Payne v. Elliott, 54 Cal. 339, Wilgus' Cases.

[5] Neiler v. Kelley, 69 Pa. St. 403; Wilkesbarre Bank v. City of Wilkesbarre, 148 Pa. 601, 24 Atl. Rep. 111; Fisher v. Essex Bank, 5 Gray 373.

[6] Burrall v. Railroad Co., 75 N. Y. 211; Ohio, etc., Co. v. Merchants, etc., Co., 11 Humph. (Tenn.) 1; Fisher v. Essex Bank, 5 Gray (Mass.) 373; Plimpton v. Bigelow, 93 N. Y. 592; Payne v. Elliott, 54 Cal. 339; Field v. Pierce, 102 Mass. 253; Spalding v. Paine, 81 Ky. 416; Jones v. Davis, 35 Ohio St. 474.

equitable, and does not give him the right of ownership to specific property of the corporation. But he does own the specific stock held in his name, and, under the rules of law, the property of the corporation is held by the corporation in trust for the stockholders.''[1]

§ 302. **Amount of capital stock.**—The charter of a corporation generally provides that the corporation shall have a certain amount of capital stock which is supposed to represent a fund upon which it obtains credit and transacts business. This fund can not be increased or decreased in amount or number of shares by the corporation without the authority of the state.[2] Stock issued in violation of this rule is void.[3] But where the power to increase exists and is irregularly exercised, the corporation is estopped to deny the validity of the stock so issued as against a bona fide holder thereof.[4] The manner in which a corporation may change the amount of its capital stock is commonly provided by the general corporation laws of the state. As a general rule, it must be exercised by the stockholders and not by the directors.[5] But where the directors have power to determine the amount of capital stock, they have power to increase the same. The rule that a corporation has no implied power to increase the amount of its capital stock when the charter has definitely fixed it at a certain sum, has no application when the charter does not impose any limitation but expressly authorizes the amount to be determined by by-law. Under such circumstances the increase may be under the authority of a by-law, and a mere resolution of the

[1] Bridgman v. Keokuk, 72 Iowa 42, per Beck, J.

[2] Scoville v. Thayer, 105 U. S. 143; Sutherland v. Olcott, 95 N. Y. 93; Grangers, etc., Co. v. Kamper, 73 Ala. 325; Crandall v. Lincoln, 52 Conn. 74; Chicago, etc., R. Co. v. Allerton, 18 Wall. (U. S.) 233; Einstein v. Rochester, etc., Co, 146 N. Y. 46; Ross-Meehan Co. v. Southern Iron Co., 72 Fed. Rep 957; Jones v. Concord, etc., R. Co., 67 N. H. 119, 234.

[3] Scoville v. Thayer, 105 U. S. 143; New York, etc., R. Co. v. Schuyler, 34 N. Y. 30.

[4] Veeder v. Mudgett, 95 N. Y. 295; Sayles v. Brown, 40 Fed. Rep. 8.

[5] Chicago, etc., Co. v. Allerton, 18 Wall. (U.S.) 233; Eidman v. Bowman, 58 Ill. 444, 11 Am. Rep. 90; Tshumi v. Hills, 6 Kan. App. 549, 51 Pac. Rep. 619.

members is a sufficient by-law for that purpose.[1] As in all other cases where there is no lack of original power, the stockholders may by acquiescence deprive themselves of the right to object to the exercise of such power by the board of directors.[2] But the reduction of the capital is a different matter. "Different questions of public policy are involved by a power of diminishing capital invested in said companies. The rights of creditors would be affected by a decrease. Their rights are not injuriously affected by an increase. To decrease the capital of such a corporation would be in most cases to withdraw capital pledged to the fortunes of the venture. These reasons have led the courts with great unanimity to hold that the power of increasing the capital does not involve or imply the power to decrease it."[3] The purchase of shares of its own stock by a corporation having authority to do so does not operate as a reduction of the capital stock, when it did not reserve to itself the power to reduce the capital stock.[4] Where the law required that the constating instrument shall state the amount of capital stock and it stated the amount and added that it might be increased, the latter provision was treated as a nullity and the amount so named as the limit.[5] In order to make this rule effective, the courts hold that stock issued in excess of the lawful amount is void and the holders of such stock do not become members of the corporation.[6] A corporation which has been directed by the court to issue a certain amount of stock to different persons, the aggregate of which exceeds the amount authorized by its charter, should issue a proportional amount to each.[7]

[1] Peck v. Elliott, 79 Fed. Rep. 10, 47 U. S. App. 605, 38 L. R. A. 616.

[2] Bailey v. Champion, etc., Co., 77 Wis. 453.

[3] Peck v. Elliott, *supra;* Sutherland v. Olcott, 95 N. Y. 94. A corporation which has completed its organization, except filing the certificate that its organization is complete, may reduce its capital stock before filing the certificate. Gade v. Forest, etc., Co., 165 Ill. 367.

[4] Western, etc., Co. v. DesMoines Nat'l Bank, 103 Iowa 455.

[5] Grangers, etc., Co. v. Kamper, 73 Ala. 325.

[6] Cartwright v. Dickinson, 88 Tenn. 476, 7 L. R. A. 706.

[7] Clark Co. v. Winchester, etc., Co. (Ky.), 43 S. W. Rep. 716. As to es-

§ 303. **Dividend stock.**—When a corporation has not issued all its stock or has authority to increase its capital stock, and there is no statutory or constitutional prohibition,[1] it may issue new shares as dividends when an amount of money or property equivalent in value to the full par value of the stock so issued has been accumulated and permanently added to the capital of the corporation.[2] "There is no public policy which in all cases condemns such dividends. Shares having been legally brought into existence may be distributed among the stockholders of a company. By such distribution no harm is done to any one person, provided the dividend is not a mere inflation of the stock of the company, with no corresponding value to answer to the stock distributed. It may be that a distribution of stock gratuitously to the stockholders of a company based upon no values, a mere inflation, or, to use a phrase much in vogue, a watering of stock, would be condemned by the law. But when stock has been lawfully created, and is held by a corporation, which it has a right to issue for value, then a stock dividend may be made, provided that the stock always represents value. * * * So long as every dollar of stock issued by a corporation is represented by a dollar of property, no harm can result to individuals or the public from distributing the stock to the stockholders. Here there was no fraud, no conspiracy, no unlawful combination * * * and we know of no principle of law, no public policy, and no statute that condemns a stock dividend under such circumstances."[3]

toppel of certain stockholders to assert invalidity of an unauthorized issue of stock, see Peter v. Union, etc., Co., 56 Ohio St. 181.

[1] See Comw. v. Boston, etc., R. Co., 142 Mass. 146.

[2] Williams v. Western Union, etc., Co., 93 N. Y. 162; Leland v. Hayden, 102 Mass. 542; Gibbons v. Mahon, 4 Mackey 130. "Corporations frequently make a dividend of this character when improvements of the corporate property or extensions of the business have been made out of the profits earned. It is also made when the corporate plant has increased in value and it seems better to issue new stock to represent the excess of value than to sell the increase and declare a cash dividend. In this country these dividends are frequently made and are constantly sustained by the courts." Cook I, § 536.

[3] Williams v. Western Union, etc., Co., 93 N. Y. 162, citing many cases.

It is discretionary with the directors whether they will declare a stock or cash dividend.[1]

§ 304. **Stock certificates.**—A certificate of stock is a written acknowledgment by the corporation of the interest of the stockholder in the corporate property and franchises. The stock must be distinguished from the certificate of stock. The former is the substance, while the latter is simply the evidence.[2] The possession of a certificate is not necessary to constitute a person a member of the corporation.[3] A stockholder has a right to demand and receive a stock certificate, but the possession of a certificate is not necessary to entitle him to enjoy the rights and privileges of membership in a corporation nor to impose upon him the duties and liabilities incidental to such membership.[4] An action may be brought against him upon a stock subscription, although no certificate has been delivered or tendered, unless the contract provides otherwise.[5]

§ 305. **Not negotiable instruments.**—Certificates of stock are not negotiable instruments,[6] although they are sometimes

[1] Howell v. Chicago, etc., R. Co., 51 Barb. (N.Y.) 378; Jackson v. Newark, etc., Co., 31 N. J. L. 277; Williams v. Western Union, etc., Co., *supra*.

[2] Cartwright v. Dickson, 88 Tenn. 476, 17 Am. St. Rep. 910; Hawley v. Brumagin, 33 Cal. 394; Payne v. Elliott, 54 Cal. 339; Hubbell v. Drexel, 11 Fed. Rep. 115.

[3] Walter A. Wood, etc., Co. v. Robbins, 56 Minn. 48; Wemple v. Railroad Co., 120 Ill. 196; Mitchell v. Beckman, 64 Cal. 117.

[4] National Bank v. Watsontown Bank, 105 U. S. 217; First Nat'l Bank v. Gifford, 47 Iowa 575; Colfax, etc., Co., v. Lyon, 69 Iowa 683; Buffalo, etc., R. Co. v. Dudley, 14 N. Y. 336; Chester, etc., Co. v. Dewey, 16 Mass. 94; Wemple v. Railroad Co., 120 Ill. 196; Columbia, etc., Co. v. Dixon, 46 Minn. 463.

[5] Marson v. Deither, 49 Minn. 423; Courtright v. Deeds, 37 Iowa 503.

[6] O'Herron v. Gray, 168 Mass. 573, 40 L. R. A. 498; Shaw v. Spencer, 100 Mass. 382; Sewall v. Boston, etc., Co., 4 Allen (Mass.) 277; East Birmingham, etc., Co. v. Dennis, 85 Ala. 565, 7 Am. St. Rep. 73; Hammond v. Hastings, 134 U. S. 401; Parker v. Sun, etc., 42 La. An. 1172; Weaver v. Barden, 49 N. Y. 286; Winter v. Belmont, etc., Co., 53 Cal. 428; Weyer v. Second Nat'l Bank, 57 Ind. 198; Young v. South, etc., Co., 85 Tenn. 189, 4 Am. St. Rep. 752; Clark v. American, etc., Co., 86 Iowa 436, 17 L. R. A. 557. "Corporate stock is not commercial paper, and it has none of the privileges and immunities which such paper has. A purchaser takes it subject to any debt due from the stock he purchases to the corpora-

said to be *quasi* negotiable,[1] and the holders are often protected through the application of the doctrine of estoppel.[2] To such an extent has the law of estoppel been applied to protect a bona fide purchaser of stock that he is protected in almost every instance where he would be protected if he were the purchaser of a promissory note or other negotiable instrument.

I. Classes of Stock.

§ 306. **Different kinds of stock.**—Corporations often issue different kinds or classes of stock, which are known by names which illustrate their principal characteristics. Thus, we find stock which is described as common, preferred, preference or preferential, guaranteed and bonus. Preferred stock is so called because the holders are entitled to a preference over the holders of the common stock in the matter of dividends. When the payment is guaranteed without reference to earnings, stock is known as guaranteed stock. The phrase "watered stock" is commonly used to describe issues which have no proper basis of property back of them, while bonus stock is stock which is issued gratuitously, without consideration. Some states provide for the issue of special kinds of stock. Thus, in Massachusetts, certain corporations may issue what is known as special stock, the holders of which are creditors of the corporation and not stockholders.[3]

tion." Gilfillan, C. J., In re People's, etc., Co., 56 Minn. 180. See note to 4 Am. St. Rep. 759. "Certificates of stock are not securities for money in any sense, much less are they negotiable securities. They are simply the muniments and evidence of the holder's title to a given share in the property and franchises of the corporation of which he is a member." Mechanic's Bank v. N. Y. Cent. R. Co., 13 N. Y. 599, 627.

[1] Daniel Neg. Inst. II, § 1708.

[2] Woods App., 92 Pa. St. 379.

[3] The Massachusetts statute (Public Stats., ch. 106, §§ 42–61) provides for what is called "special stock." In American, etc., Works v. Boston, etc., Co., 139 Mass. 5, 9, the court in discussing this stock says: "It is limited in amount to two-fifths of the actual capital; it is subject to redemption by the corporation at par after a fixed time, to be expressed in certificates; the corporation is bound to pay a fixed half-yearly sum or dividend upon it as a debt; the holders of it are in no event liable for the debts of the corporation beyond their stock; and the issue of special stock makes all the general stockholders liable for all the debts and contracts of the cor-

§ 307. **Preferred stock.**—The only kind of stock other than common entitled to any particular consideration at this time, is that which is known as preferred. Ordinarily preferred stock is entitled to a preference in the payment of dividends before anything is paid on the common stock.[1] After the preferred dividend is paid, any additional earnings are used for the purpose of paying dividends upon the common stock. The right of further participation in this second dividend is, of course, determined by the terms of the contract between the corporation and the holders of the preferred stock. Guaranteed stock generally means nothing more than that the corporation guarantees to pay a preferred dividend upon such stock out of the earnings of the corporation, if there are any earnings. Ordinarily it does not make the holder a creditor who is entitled to the dividend without reference to earnings.

§ 308. **Power to issue preferred stock.**—As a general rule a corporation has no power to issue preferred stock after its organization, unless expressly authorized to do so by its charter or by the laws of the state.[2] But at the time of organization it may, unless prohibited by statute, provide for a preference of one class over another, in respect to both capital and dividend.[3] So, unless expressly prohibited by statute, such stock may be issued at any time by the consent of all parties affected thereby, and such consent may be inferred from the acquiescence of the stockholders.[4]

poration until the special stock is fully redeemed." The dividends upon this stock are payable without regard to earnings. Williams v. Parker, 136 Mass. 204.

[1] Totten v. Tison, 54 Ga. 139; Chaffee v. Rutland, etc., R. Co., 55 Vt. 110.

[2] Belfast, etc., R. Co. v. Belfast, 77 Maine, 445; Kent v. Quicksilver, etc., Co., 78 N. Y. 159; Campbell v. American, etc., Co., 122 N. Y. 455, 11 L. R. A. 596; Chaffee v. Rutland, etc., R. Co., 55 Vt. 110; Gordon v. Richmond, etc., R. Co., 78 Va. 501; Totten v. Tison, 54 Ga. 139; Taft v. Hartford, etc., R. Co., 8 R. I. 310; Banigan v. Bard, 134 U. S. 291; Moss v. Syers, 32 L. J. Ch. Div. (N. S.) 711; Anthony v. Household, etc., Co., 16 R. I. 571, 5 L. R. A. 575; Melhads v. Hamilton, 29 L. T. (N. S.) 364; Re South Durham, etc., Co., L. R. 31 Ch. Div. 261.

[3] Hamlin v. Toledo, etc., R. Co., 78 Fed. Rep. 664, 47 U. S. App. 422, 36 L. R. A. 826.

[4] Hazelhurst v. Savannah, etc., R. Co., 43 Ga. 13; Higgins v. Lansingh,

§ 309. **Power of majority.**—It is generally held that after the organization of the corporation the majority of the stockholders have no power to issue preferred shares without the unanimous consent of the holders of the stock then outstanding. This rule rests on the ground that such stock impairs the contracts with the original subscribers, who are entitled to share equally in the earnings of the corporation. "Shares of stock," said Folger, J.,[1] "are in the nature of choses in action and give the holder a fixed right in the division of the profits or earnings of the company so long as it exists, and of its effects when dissolved. The right is as inviolable as is any right in property, and can no more be taken away or lessened against the will of the owner than can any other right unless power is reserved in the first instance when it enters into the constitution of the right or is properly derived afterward from a superior law-giver."

§ 310. **Under legislative authority.**—The principle stated in the preceding section would prevent the legislature from authorizing the issuing of preferred stock without the unanimous consent of the existing stockholders. But, upon the theory that the issue of such stock is merely a method of borrowing money, it has been held that the power to issue it without the consent of prior stockholders may be conferred by a statute passed subsequent to the organization of the corporation and the issue of its original stock.[2] But it is only when the preferred stock takes the form of borrowing that it creates a debt, and in such cases the holders are creditors and not stockholders.[3]

154 Ill. 301; Campbell v. American, etc., Co., 122 N.Y. 455, 11 L. R. A. 596; Lockhart v. Van Alstyne, 31 Mich. 76; Kent v. Quicksilver, etc., Co., 78 N. Y. 159; Bates v. Androscoggin, etc., R. Co., 49 Maine 491.

[1] Kent v. Quicksilver, etc., Co., 78 N. Y. 159; Hutton v. Scarborough, etc., Co., 2 Drew & Sm. 521.

[2] Everhart v. Westchester, etc., R. Co., 28 Pa. St. 339; Curry v. Scott, 54 Pa. St. 270; Rutland, etc., R. Co. v. Thrall, 35 Vt. 536; Covington v. Covington, etc., Co., 10 Bush (Ky.) 69.

[3] Hazelhurst v. Railroad Co., 43 Ga. 13; Totten v. Tison, 54 Ga. 139; Westchester, etc., R. Co. v. Jackson, 77 Pa. St. 321.

§ 311. **Estoppel.**—The doctrine of estoppel may be invoked against an attack on the validity of preferred stock. It may be invoked against a corporation which has received a consideration or the stockholders who have participated[1] or acquiesced[2] in its issue. Thus one who voted for the issue of the stock and afterwards voted it at the meetings of the stockholders can not assert its invalidity after the corporation has become insolvent.[3] So one who accepted the stock in payment for work as a contractor and received interest on it for several years is estopped to deny that he is a stockholder as against the creditors of the insolvent corporation.[4]

§ 312. **Status of holders of preferred stock.**—Unless otherwise provided by statute or the charter or contract the holders of preferred shares are stockholders with the same rights and powers in the management of the corporation as the holders of the common stock[5] and subject to the same general and statutory liabilities.[6]

§ 313. **Rights of holders of preferred stock.**—The rights of the holders of preferred shares are enforcible according to the terms of their contract with the corporation.[7] The characteristic feature of such stock is the provision that the holders are entitled to payment of the full stipulated dividends before any dividends are paid on the common stock. Such dividends, however, are not payable absolutely like interest; they are payable and can be made payable legally only out of profits.[8] A

[1] Hazelhurst v. Savannah, etc., R. Co., 43 Ga. 13; McGregor v. Home, etc., Co., 33 N. J. Eq. 181.

[2] Taylor v. South, etc., R. Co., 13 Fed. Rep. 152.

[3] Banigan v. Bard, 134 U. S. 291.

[4] Branch v. Jesup, 106 U. S. 468. See Tama, etc., Co. v. Hopkins, 79 Iowa 653; Evansville, etc., R. Co. v. Evansville, 15 Ind. 395.

[5] Miller v. Ratterman, 47 Ohio St. 141; Warren v. King, 108 U. S. 389; Mackintosh v. Flint, etc., R. Co., 34 Fed. Rep. 582; Field v. Lamson, etc., Co., 162 Mass. 388; Taft v. Railroad Co., 8 R. I. 310; Belfast, etc., R. Co. v. Belfast, 77 Maine 445.

[6] Railway Co. v. Smith, 48 Ohio St. 219.

[7] Hazeltine v. Belfast, etc., R. Co., 79 Maine 411, 1 Am. St. Rep. 330, annotated.

[8] Boardman v. Lake Shore, etc., R. Co., 84 N. Y. 157; Lockhart v. Van Alstyne, 31 Mich. 76; Miller v. Ratterman, 47 Ohio St. 141; Union Pac. R. Co. v. United States, 99 U. S. 402; Taft v. Hartford, etc., R. Co., 8 R. I.

guarantee of dividends upon preferred stock in accordance with a statute permitting a guarantee of such dividends, payable cumulatively out of net profits, does not make the dividend payable absolutely. In such a case the corporation can not be compelled to declare a dividend out of net profits against the judgment of the directors.[1] The directors may, in their discretion, apply the earnings toward the payment of debts incurred during the year in enlarging a plant instead of to the payment of dividends on preferred stock.[2] Holders of such stock are not creditors of the corporation, and the stock can not be treated as an indebtedness which can be considered in determining whether its obligations are such as to prevent it from engaging in a certain enterprise.[3] An agreement to pay dividends on preferred stock out of the net earnings of the corporation does not mean the net earnings of the corporation as it was when the preferred stock was issued. The corporation may, after the agreement, incur new obligations which will diminish the net earnings applicable to such dividends.[4] A guaranty of dividends is construed to mean a guaranty that the dividends will be paid if any are earned.[5] Unless otherwise provided by statute, the holders of preferred stock are not

310. Stock bearing interest without reference to earnings is generally held invalid. Miller v. Pittsburg, etc., R. Co., 40 Pa. St. 237, 80 Am. Dec. 570; Pittsburg, etc., R. Co. v. Allegheny Co., 63 Pa. St. 126; Painsville, etc., R. Co. v. King, 17 Ohio St. 534; Ohio College v. Rosenthal, 45 Ohio St. 183; Cunningham v. Vermont, etc., R. Co., 12 Gray 411.

[1] Field v. Lamson, etc., Co., 162 Mass. 388, 27 L. R. A. 136.

[2] New York, etc., R. Co. v. Nickals, 119 U. S. 296.

[3] People v. St. Louis, etc., R. Co., 35 L. R. A. 656; Warren v. King, 108 U. S. 389; Chaffee v. Rutland R. Co., 55 Vt. 110; Taft v. Hartford R. Co., 8 R. I. 310. That preferred stock may be so issued as to amount to a debt, see Gordon's Exr's v. Railroad Co., 78 Va. 501. In Miller v. Ratterman, 47 Ohio St. 141, the court said: "The relation of the holder of preferred stock is, in some of its aspects, similar to that of a creditor; but he is not a creditor save as to dividends, after the same are declared. Nor does he sustain a dual relation to the corporation. He is either a stockholder or a creditor."

[4] St. John v. Railway Co., 22 Wall. (U. S.) 136; Warren v. King, 108 U. S. 389. But see Dent v. Tramways Co., 16 Ch. Div. 344, 2 Cum. Cas. Pri. Corp. 225.

[5] Taft v. Railroad Co., 8 R. I. 310; Miller v. Ratterman, 47 Ohio St. 141.

entitled to preference in the distribution of the capital when a corporation is wound up.[1]

§ 314. **Accumulative dividends.**—When the dividends are cumulative and accumulated earnings for any period are insufficient to pay dividends for that period, such arrears must be paid out of subsequent profits. In other words, unless declared to be non-cumulative, or there is a requirement that it shall be paid out of the net profits of the year, or that the entire net profits of the year shall be paid out in dividends,[2] all arrears on dividends on preferred stock must be paid before a dividend can be paid on common stock.[3] In Boardman v. Ry. Co., *supra*, the court says: "The reasonable and fair interpretation of the contract is that the dividends were not only to be preferred, but being guaranteed, were cumulative and a specific charge upon the accruing profits, to be paid as arrears, before any other dividends were divided upon the common stock. The doctrine that preference shares are entitled to be first paid the amount of dividends guaranteed and of all arrears of dividends and interest before the other shareholders are entitled to receive anything, and although they can receive no profits where none are earned, yet, as soon as there are any profits to divide, they are entitled to the same, is fully supported by authority."[4]

[1] McGregor v. Home, etc., Co., 33 N. J. Eq. 181; Gordon v. Richmond, etc., R. Co., 78 Va. 501.

[2] Railroad Co., v. Belfast, 77 Maine 445; Hazeltine v. Belfast, etc., R. Co., 79 Maine 411, 1 Am. St. Rep. 330; New York, etc., R. Co. v. Nichals, 119 U. S. 296.

[3] Boardman v. Lake Shore, etc., R. Co., 84 N. Y. 157; Elkins v. Camden, etc., R. Co., 36 N. J. Eq. 233; Bailey v. Hannibal, etc., R. Co., 17 Wall. 96, 1 Dillon (C. C.) 174; Henry v. Great Northern R. Co., 1 DeG. & J. 606; Harrison v. Mexican R. Co., L. R. 19 Eq. 358; *contra* by statute, 26–27 Vict., ch. 118, § 14; Lockhart v. Van Alstyne, 31 Mich. 76, 18 Am. Rep. 156; Prouty v. Michigan, etc., R. Co., 1 Hun (N. Y.) 655; Wood v. Lary, 47 Hun (N. Y.) 550.

[4] Adams v. Ft. Plain Bank, 36 N. Y. 255. Ordinarily, preferred shareholders are entitled "to have deficiencies in their dividends made up out of the earnings legally applicable to the payment of dividends, whenever such earnings are received, in preference to any payment to the holders of the common stock. This right is inferred from the contract, and need not be provided for in express terms. Corry v. Londonderry, etc., R. Co., 29 Beav. 263, 7 Jur. (N. S.) 508, 30 L. J. Ch. 290."

II. Nature of Capital Stock.

§ 315. **Personal property.**—By the older law shares of stock were considered real or personal property, according to the nature, object and manner of the investment.[1] But these decisions are now practically obsolete, and it may be taken as the settled law that shares of stock are personal property.[2] They are in the nature of choses in action.[3] At common law such shares belonging to a wife do not vest in the husband.[4] Upon the death of the holder of stock in a corporation, the property of which consists of real estate, the shares are distributed as personal property.[5]

§ 316. **Statute of frauds.**—The American decisions generally hold that the 17th section of the statute of frauds, which requires that every contract for the sale of goods, wares and merchandise of a specified value shall be in writing, applies to a sale of shares of stock.[6] Modern English authorities hold

[1] Greenleaf's Ed. Cruise on Real Property, 39; Tomlinson v. Tomlinson, 9 Beav. 459; Price v. Price, 6 Dana (Ky.) 107; Copeland v. Copeland, 7 Bush (Ky.) 349; Wells v. Cowles, 2 Conn. 567; Johns v. Johns, 1 Ohio St. 250, where the cases are fully reviewed by Thurman, J.

[2] Lowndes v. Cooch, 87 Md. 478, 40 L. R. A. 380; Wilkesbarre v. City of Wilkesbarre, 148 Pa. 601, 24 Atl. Rep. 111; Payne v. Elliott, 54 Cal. 339; San Francisco v. Flood, 64 Cal. 504; Tregear v. Etiwanda, etc., Co., 76 Cal. 537, 9 Am. St. Rep. 245; Cooper v. Corbin, 105 Ill. 224; Seward v. Rising Sun, 79 Ind. 351; Arnold v. Ruggles, 1 R. I. 165; Dyer v. Osborne, 11 R. I. 321; Baldwin v. Canfield, 26 Minn. 43. Except in Pennsylvania (Neiler v. Kelley, 69 Pa. St 403), trover lies for the conversion of shares of stock. Payne v. Elliott, 54 Cal. 339; Ayers v. French, 41 Conn. 142; McAllister v. Kuhn, 96 U. S. 87.

[3] Fisher v. Bank, 5 Gray (Mass.) 373.

[4] Arnold v. Ruggles, 1 R. I. 165.

[5] Russell v. Temple (Mass.), 3 Dane's Abr. 108.

[6] In Tisdale v. Harris, 20 Pick. (Mass.) 9, Chief Justice Shaw says: "There is nothing in the nature of shares of stock in companies which in reason or sound policy should exempt contracts in respect to them from this reasonable restriction, designed by the statute to prevent frauds in the sale of other commodities. On the contrary, these companies have become so numerous, so large an amount of the property of the community is invested in them; and as the ordinary indicia of property arising from delivery and possession can not take place, there seems to be a peculiar reason for extending the provision of this statute; and thus they may properly be included under the term 'goods,' as they are within the reason and policy of

that this section has no application,[1] and this rule is adopted by some American cases.[2] In some states the statutes use the words "personal property," and expressly include choses in action.[3] An agreement for the sale of shares in a corporation owning real estate is not an agreement for the sale of an interest in land, and need not be in writing.[4]

§ 317. **The trust fund theory.**—A long line of American decisions establishes the doctrine that after insolvency the capital of a corporation as represented by its subscribed capital stock is a trust fund pledged for the payment of the debts of the corporation.[5] The doctrine has been applied in cases where the

the act. The court is of the opinion that contracts for the sale of shares, in the absence of other requisites, must be proved by some note or memorandum in writing." Mason v. Decker, 72 N. Y. 595; Boardman v. Cutter, 128 Mass. 388; Mayer v. Child, 47 Cal. 142; North v. Forest, 15 Conn. 400; Pray v. Mitchell, 60 Maine 430; Greenwood v. Law, 55 N. J. L. 168; Hudson v. Weir, 29 Ala. 294; Green v. Brokins, 23 Mich. 48; Reed, Statute of Frauds, § 234.

[1] Humble v. Mitchell, 11 Ad. & El. 205; Colonial Bank v. Whinney, 30 Ch. Div. 261; Knight v. Barber, 16 Mee. & W. 66.

[2] Webb v. Railroad Co., 77 Md. 92; Whittemore v. Gibbs, 24 N. H. 484; Vawter v. Griffin, 40 Ind. 593.

[3] See Peabody v. Speyers, 56 N. Y. 230; Mayer v. Child, 47 Cal. 142; Spear v. Bach, 82 Wis. 192; Southern, etc., Co. v. Cole, 4 Fla. 359.

[4] § 315, *supra*.

[5] Wood v. Dummer, 3 Mason 308; Sawyer v. Hoag, 17 Wall. 610; Upton v. Tribilcock, 91 U. S. 45; Sanger v. Upton, 91 U. S. 56; Webster v. Upton, 91 U. S. 65; Chubb v. Upton, 95 U. S. 665; Pullman v. Upton, 96 U. S. 328; Graham v. Railroad Co., 102 U. S. 148; Morgan Co. v. Allen, 103 U. S. 498; Richardson v. Green, 133 U. S. 30; Handley v. Stutz, 139 U. S. 417; Clark v. Bever, 139 U. S. 96; Fogg v. Blair, 139 U. S. 118; Camden v. Stuart, 144 U. S. 104; Wabash, etc., R. Co. v. Ham, 114 U. S. 587; Alling v. Wenzel, 133 Ill. 264; Thompson v. Reno Sav. Bank, 19 Nev. 242, 3 Am. St. Rep. 797; Marshall, etc., Co. v. Killian, 99 N. C. 501, 6 Am. St. Rep. 539; Bartlett v. Drew, 57 N. Y. 587; State v. Com. Bank, 28 Neb. 677. In Sanger v. Upton, 91 U. S. 56, the doctrine is stated as follows: "The capital stock of an incorporated company is a fund set apart for the payment of its debts. It is a substitute for the personal liability which subsists in private copartnerships. When debts are incurred, a contract arises with the creditors that it shall not be withdrawn or applied otherwise than upon their demands, until their demands are satisfied. The creditors have a lien upon it in equity. If divested they may follow it as far as it can be traced, and subject it to the payment of their claims, except as against holders who have taken it bona fide for a valuable consideration and without notice. It is publicly pledged to those who deal with the corporation, for their security. Unpaid stock is as

corporation had distributed its capital among the stockholders without providing for the payment of creditors, where the corporation released the subscribers from their liability to contribute their share of the capital stock, and where it has transferred the corporate property to third persons in fraud of its creditors. In a case of the latter character, the court said: "The assets of a corporation are a trust fund for the payment of its debts, upon which the creditors have an equitable lien, both as against the stockholders and all transferees except those purchasing in good faith for value."[1]

It is the settled doctrine of the supreme court of the United States that "the capital stock of an insolvent corporation is a trust fund for the payment of its debts, that the law implies a promise by the original subscribers of stock, who did not pay for it in money or other property, to pay for the same when called upon by the creditors; and that a contract between themselves and the corporation, that the stock shall be treated as fully paid and non-assessable, or otherwise limiting their liability, therefore is void against creditors."[2]

But there is no direct and express trust attached to the property of a corporation. It is not "in any true and complete sense a trust, and can only be called so by way of analogy or metaphor."[3] The true meaning of the phrase has recently

much a part of this pledge, and as much a part of the assets of the company, as the cash which has been paid in upon it. Creditors have the same right to look to it as to anything else, and the same right to insist upon its payment as upon the payment of any other debt due to the company. As regards creditors, there is no distinction between such a demand and any other assets which may form a part of the property and effects of the corporation."

[1] Cole v. Millerton, etc., Co., 133 N. Y. 164. See, also, Sutton, etc., Co. v. Hutchinson, 63 Fed. Rep. 496, 11 C. C. A. 320.

[2] Handley v. Stutz, 139 U. S. 417. Certain decisions having given rise to suspicion that the court was wavering in its adherence to this doctrine, in the recent case Camden v. Stuart, 144 U. S. 104, Mr. Justice Brown said: "Nothing that was said in the recent cases of Clark v. Bever, 139 U. S. 96; Fogg v. Blair, 139 U. S. 118, or Handley v. Stutz, 139 U. S. 417, was intended to overrule or qualify in any way the wholesome principle adopted by this court in the earlier cases, especially as applied to the original subscribers to stock."

[3] Pomeroy, Eq. Jur. II, § 1046; Gra-

been stated by the supreme court in a case in which simple contract creditors came into a court of equity and asked to have the corporate property subjected to a lien in their favor. The court said: "While it is true language has been frequently used to the effect that the assets of a corporation are a trust fund held by a corporation for the benefit of creditors, this has not been to convey the idea that there is a direct and express trust attached to the property. * * * The corporation is an entity distinct from its stockholders as from its creditors. Solvent, it holds its property as any individual holds his, free from the touch of a creditor who has acquired no lien; free, also, from the touch of a stockholder who, though equitably interested in, has no legal right to, the property. Becoming insolvent, the equitable interest of the stockholders in the property, together with their conditional liability to the creditors, places the property in a condition of trust, first for the creditors, and then for the stockholders. Whatever of trust there is arises from the peculiar and diverse equitable rights of the stockholders as against the corporation in its property, and their conditional liability to its creditors. It is rather a trust in the administration of the assets after possession by a court of equity, than a trust attaching to the property as such, for the direct benefit of either creditor or stockholder."[1] The theory has no application until the corporation becomes insolvent.[2]

§ 318. **Meaning of the doctrine.**—But this doctrine does not mean all that the language used in some of the decisions would seem to imply. It is only in a limited sense that the capital stock is a trust fund. No direct and express trust attaches to the property of a corporation. As stated above it is not "in any true and complete sense a trust and can only be

ham v. Railroad Co., 102 U. S. 148; Hollins v. Brierfield, etc., Co., 150 U. S. 371. As to what constitutes a withdrawal of corporate assets, see Buck v. Ross, 68 Conn. 29, 57 Am. St. Rep. 60; In re Brockway, etc., Co., 89 Me. 121, 56 Am. St. Rep. 401.

[1] Hollins v. Brierfield, etc., Co., 150 U.S.371. The limitations upon the general language used in some of the cases are also stated in Graham v. Railroad Co., 102 U. S. 148; Fogg v. Blair, 133 U. S. 534, 541; Railroad Co. v. Ham, 114 U. S. 587.

[2] Fear v. Bartlett, 81 Md. 435, 33 L. R. A. 721.

called so by way of analogy or metaphor."[1] Thus the rule that where a creditor has a trust in his favor, or a lien upon property for a debt due him, he may go into equity without exhausting his legal remedies, does not apply,[2] because, as above stated, there is no "true and complete trust." The general creditors of a corporation have no lien upon the property of the corporation by virtue of the doctrine that the capital stock is a trust fund for the protection of creditors. Hence a party may deal with a corporation in respect to its property in the same manner as with an individual owner, and with no greater danger of being held to have received into his possession property burdened with a trust or lien. As between a corporation and its creditors, a corporation is simply a debtor and does not hold its property in trust or subject to a lien in their favor in any other sense than does an individual debtor.[3]

The trust fund doctrine only means that the property of the corporation must first be appropriated to the payment of the debts of the company before any portion can be distributed to the stockholders; it does not mean that the property is so affected by the indebtedness of the company that it can not be sold, transferred, or mortgaged to bona fide purchasers for a valuable consideration, except subject to the liability of being appropriated to pay that indebtedness.[4] Such a doctrine has no existence. If it was a real trust fund it would be applicable to the payment of all the debts of the corporation, but it is well settled that only those who became creditors before the date of the transaction complained of, and who at least presumptively relied on the credit of the fund, can be heard to question its validity.[5]

But when "a corporation becomes insolvent, it is so far civilly dead that its property may be administered as a trust fund for the benefit of its stockholders and creditors: a court of

[1] Pomeroy Eq. Jur. II, § 1046; Hollins v. Brierfield, etc., Co., 150 U. S. 371; O'Bear, etc., Co. v. Volfer & Co., 106 Ala. 205, 28 L. R. A. 707.

[2] Case v. Beauregard, 101 U. S. 688.

[3] Hollins v. Brierfield, etc., Co., 150 U. S. 371 (1893); Read v. Cumberland, etc., Co., 93 Tenn. 482, 27 S. W. Rep. 660.

[4] Fogg v. Blair, 133 U. S. 534 (1890).

[5] First Nat'l Bank v. Gustin, etc., Co., 42 Minn. 327; Hospes v. Northwestern, etc., Co., 48 Minn. 174.

equity, at the instance of the proper parties, will then make these funds trust funds, which in other circumstances are as much the absolute property of the corporation as any man's property is his.'"[1]

§ 319. **Criticisms.**—While this doctrine seems to be established in the jurisprudence of the United States, it has never been recognized by the English courts,[2] and has been characterized in recent American decisions as a confusing device for accomplishing ends more readily attainable on well established and easily comprehended principles.[3] It is apparent, from what has already been said, that it is little more than a formula, and signifies that the corporation must preserve its property for the payment of its debts to creditors who have become such in reliance upon the apparent means provided for that purpose. It is difficult to see why this does not apply to one individual as well as to a corporation. In a well considered Minnesota case, in which the whole doctrine is virtually repudiated, Mr. Justice Michell said:[4] "The phrase that the capital of a corporation constitutes a trust fund for the benefit of creditors is misleading. Corporate property is not held in trust, in any proper sense of the term. A trust implies two estates or interests—one equitable and one legal—one person as trustee, holding the legal title, while another as *cestui que trust*, has the beneficial interest. Absolute control and power of disposition are inconsistent with the idea of a trust. The capital of a corporation is its property. It has the whole beneficial interest in it as well as the legal title. It may use the income and profits of it, and sell and dispose of it the

[1] Graham v. Railroad Co., 102 U. S. 148, 160; Hollins v. Brierfield, etc., Co., 150 U. S. 371; Railroad Co. v. Ham, 114 U. S. 587.

[2] Creditors "can obtain nothing but what the company can get from the shareholders." In re Dronfield, etc., Co., 17 Ch. Div. 76; In re Ambrose, etc., Co., 14 Ch. Div. 390. The price to be paid for shares is a matter of contract irrespective of the face value. Guest v. Worcester R. Co., L. R. 4 C. P. 9. But contracts for the sale of stock below par are by statute required to be in writing and registered with the registrar of joint stock companies.

[3] Hospes v. Northwestern, etc., Co., 48 Minn. 174; Brant v. Ehlen, 59 Md. 1.

[4] Hospes v. Northwestern, etc., Co., 48 Minn. 174.

same as a natural person. It is a trustee for the creditors in the same sense and to the same extent as a natural person, but no further.'' In the opinion of the court, all the cases in which the trust fund theory has been advanced could have been equally well founded on the simple doctrine of fraud. ''By putting it on the ground of fraud, and applying the old and familiar rules of law on that subject to the peculiar nature of a corporation, and the relation which its stockholders bear to it and to the public, we have at once rational and logical ground on which to stand. The capital of a corporation is the basis of its credit. It is a substitute for the individual liability of those who own its stock. People deal with it and give it credit on the faith of it. They have a right to assume that it has paid in capital to the amount which it represents itself as having, and if they give it credit on the faith of that representation, and if the representation is false, it is a fraud upon them, and, in case the corporation becomes insolvent, the law upon the plainest principles of common justice says to the delinquent stockholder: 'Make that representation good by paying for your stock.' It certainly can not require the invention of any new doctrine in order to enforce so familiar a rule of equity.''

III. Fraudulently Issued Stock.

§ 320. **Overissue of stock.**—Stock issued accidentally or fraudulently in excess of the limit fixed by law is invalid, even in the hands of a bona fide purchaser for value,[1] and the corporation may have it declared void and ordered canceled.[2] The holding of such stock confers no rights of membership upon the holder; he does not become a stockholder[3] and is not liable on his subscription as such.[4]

§ 321. **Bona fide holders of fraudulently issued stock.**—A bona fide holder of fraudulently issued stock, which is represented by certificates signed by the corporation officers having

[1] Scoville v. Thayer, 105 U. S. 143; Bank v. Kurtz, 99 Pa. St. 344; Mt. Holly, etc., Company's App., 99 Pa. St. 513.

[2] New York, etc., R. Co. v. Schuyler, 34 N. Y. 30.

[3] Arkansas, etc., Co. v. Farmers', etc., Co., 13 Colo. 587.

[4] Clark v. Turner, 73 Ga. 1.

authority to issue stock and actually issued by such officers, may recover damages sustained by reason of the issue of such stock from the corporation.[1] Under such circumstances the corporation is estopped to deny its liability for loss arising from the worthless character of the certificates issued by the acts of its officers within the apparent scope of their authority. Information given by a person in charge of the office of a corporation that a certain certificate of stock is genuine and in a condition for transfer was held to estop the corporation from denying its liability to indemnify the transferee against loss, because of its spurious character.[2] The corporation is liable to any one injured by reason of the spurious character of the certificate. Merely directing an employe to cancel surrendered certificates gives him neither express nor implied authority to reissue them, and the corporation, in such a case, is not liable for damages caused by their wrongful use to secure a personal loan.[3] The liability in such cases rests upon the principle that the acts of a corporation through its officers of issuing spurious certificates of stock, when accepted and acted upon by another in good faith, estops the corporation from denying its liability to the bona fide taker of the shares for the loss that he has thereby sustained.

§ 322. **Estoppel by recital in stock certificate.**—A stock certificate issued by a corporation having power to issue it, in which it is stated that a designated person is the owner of a certain number of shares, transferable only on the books of the corporation on the indorsement and surrender of the certificate, is a continuing affirmation as to the ownership of stock, and that the corporation will not transfer the stock upon its books unless the certificate is first surrendered. Such a certificate is an assurance to the commercial world that the shares of stock are the property of the person designated and that he has the power and right to transfer and sell the stock until this power and right have been lawfully terminated.

[1] New York, etc., R. Co. v. Schuyler, 34 N. Y. 30; Allen v. South Boston, etc., R. Co., 150 Mass. 200, 15 Am. St. Rep. 185.

[2] Jarvis v. Manhattan Beach Co., 148 N. Y. 652, 31 L. R. A. 776.

[3] Knox v. Eden, etc., Co., 148 N. Y. 441, 31 L. R. A. 779.

Such a representation tends to enhance the value of the stock, and must be presumed to have been made with the expectation that it would be acted upon by others.[1] In an action against the officers who fraudulently issued stock certificates, the court said, with reference to the certificates: "They authenticated them, fraudulently and falsely attested them as genuine. They bore on their face such false attestation, which was equivalent to an assertion on their part to all persons who should purchase or to whom they should be offered that they were genuine. In this way they invited confidence and induced trade. These acts were done with intent to defraud any and all purchasers, well knowing that any person to whose hands these false certificates should come by fair purchase might be injured. Therefore, having authenticated and issued these certificates for the purpose of defrauding, these defendants should be held liable to anyone sustaining damage by purchasing on the faith of their genuineness.[2] It has been held that fraudulent certificates are not misrepresentations to the general public but to the original grantees only, upon the principle that an admission or representation is no estoppel in favor of a stranger.[3] But "it is believed that the courts have gone far enough to establish a rule precisely the contrary."[4]

§ 323. **Liability for fraudulent acts of agents.**—By the application of the ordinary rule of *respondeat superior*, a corporation is liable in damages to one who has been defrauded by the act of an agent or officer of a corporation in issuing fictitious stock.[5] If the issue of the stock is within the power of the corporation, the recitals in its certificate are binding upon the corporation and it is obliged to admit the innocent holder of the certificate to the rights of a stockholder.[6] So the corpo-

[1] Joslyn v. St. Paul, etc., Co., 44 Minn. 183; Cincinnati, etc., R. Co. v. Citizens' Nat'l Bank, 56 Ohio St. 351, 43 L. R. A. 777.

[2] Bruff v. Mali, 36 N. Y. 200.

[3] Mechanics' Bank v. New York, etc., R. Co., 13 N. Y. 599.

[4] Thompson Priv. Corp., § 1500, citing Eaton, etc., Co. v. Avery, 83 N. Y. 31, 38 Am. Rep. 389, as establishing this principle in connection with the liability of commercial agencies.

[5] Jarvis v. Manhattan, etc., Co., 148 N. Y. 652, 31 L. R. A. 776.

[6] Cincinnati, etc., Co. v. Citizens' Nat'l Bank, 56 Ohio St. 351; Manhat-

ration, by failing to act promptly, may lose the right which, under some circumstances, it might have, to have fraudulent shares surrendered up and canceled. By acquiescence it is held to have ratified the issue.[1] But, when there is an over-issue of shares, the holder acquires no rights as a stockholder, and any holder of genuine shares may maintain a suit in equity to have the illegal shares canceled or to prevent the corporation from in any way recognizing them.[2] A distinction has been made between a case where the fraudulent issue was made by the agent for his own benefit, and where it was made by him while acting for the corporation. In the former case it is held that the holder of the certificate had no right of action against the corporation for damages, on the theory that the purchaser of a non-negotiable instrument takes only the title of the seller.[3] But this position does not seem to be supported by the best authorities. Where the agent issues the stock fraudulently to persons who are dealing with the corporation through him, there is no doubt as to the liability of the corporation for damages caused to a bona fide holder. In the well-known Schuyler cases it appears that Schuyler was the president and director of the company, and for many years acted as its transfer agent at New York city, under an appointment general in terms. During this time he issued great numbers of fraudulent overissued certificates, and the corporation was held liable in damages to the holders. It was held that the false certificates and fraudulent transfers did not create valid stock of the corporation as "a corporation with a fixed capital divided into a fixed number of shares can have no power of its own volition, or by any act of its officers or agents to enlarge the capital or increase the number of shares into which it is divided;" that if such a result can not be ac-

tan, etc., Co. v. Harned, 27 Fed. Rep. 484.

[1] American, etc., Co. v. Bayless, 91 Ky. 94.

[2] Campbell v. Morgan, 4 Ill. App. 100; Underwood v. N. Y., etc., R. Co., 17 Howard's Practice N. Y. 537.

[3] See Tome v. Ry. Co., 39 Md. 36, 17 Am. Rep. 540; Willis v. Fry, 13 Phila. 33; Mechanics' Bank v. N. Y., etc., R. Co., 13 N. Y. 599; overruled by N. Y., etc., R. Co. v. Schuyler, 34 N. Y. 30, and see Titus v. Great Western, etc., Co., 61 N. Y. 237.

complished directly, "it is absurd to suppose that it can be produced by the covert or fraudulent efforts of one or more of the agents of the corporation."[1] Fraudulently issued stock certificates may, however, by estopped bind the corporation either to indemnify, or issue valid certificates to, one who, in good faith, relies upon the act of the corporation in issuing them.[2] The corporation is liable in damages if a certificate of stock is fraudulently issued to a purchaser by its treasurer with whom blank certificates signed by the president have been left.[3] Stock certificates issued by the officers of the corporation with apparent authority, fraudulently or by mistake, which do not amount to an overissue, are valid as against the corporation in the hands of bona fide purchasers.[4]

§ 324. **Fraudulent acts of agents, continued.**—The liability of a corporation, on stock fraudulently issued by its officers, was recently given careful consideration by the supreme court of Ohio.[5] The conclusion was that one who purchases a cer-

[1] N. Y., etc., R. Co. v. Schuyler, 34 N. Y. 30.

[2] Appeal of Kisterbock, 127 Pa. St. 601, 14 Am. St. Rep. 868.

[3] Allen v. South Boston, etc., R. Co., 150 Mass. 200, 15 Am. St. Rep. 185.

[4] Fifth Avenue Bank v. Forty-second Street, etc., Ferry R. Co., 137 N. Y. 231, 33 N. E. Rep. 378; Farrington v. Railroad Co., 150 Mass. 406; Tome v. Railroad Co., 39 Md. 36; 17 Am. Rep. 540.

[5] Cincinnati, etc., Co. v. Citizens' Nat'l Bank, 56 Ohio St. 351, 43 L. R. A. 777. The court said: "In some of the cases importance has been attached to the negligence of the company, through its proper agents, in not supervising the conduct of its business, and whereby the particular agent has been enabled to perpetrate his frauds. But I apprehend that, upon an accurate analysis of the company's liability in such a case, it will be found to rest on its liability for the acts of the agent who perpetrated the fraud. If the extent of his agency included the legitimate doing of an act of the kind done, then it will be liable, though the act done was a fraud as to it and other persons. As to an innocent third person, affected by the agent's wrongful act, the negligence of the company in not discovering or preventing the fraud may accentuate his right of recovery, but does not, as I apprehend, add to nor create that right.

"The plaintiff in error relies much upon the case of Moores v. Citizens' Nat'l Bank, 111 U. S. 156, 28 L. ed. 385. We think it sufficient to distinguish that case from this that the court there found that the plaintiff made the cashier of the bank, who committed the fraud, her agent to procure and have transferred to her the stock on which she proposed to loan him the money, and that in doing so he acted for her, and not the bank; and, therefore, that she, and not the bank, was responsible for his wrong-

tificate of stock which is in the usual form, without knowledge of any fraud in its issue, is entitled to have it transferred to him on the books of the company, or upon demand and refusal to transfer, is entitled to recover its value at the time of the demand. Where certificates of stock are required to be issued by

ful act in filling up the certificate in fraud of the bank as well as of the plaintiff. If the court was right in its assumption as to the fact of agency, then the decision can have no application to this case, because there is no such feature in it. * * *

"It may be further observed that the case does not seem to be in harmony with Allen v. South Boston R. Co., 150 Mass. 200, 5 L. R. A. 716, where, on a state of facts quite similar, the court held the treasurer who committed the frauds to be the agent of the company, and not of the party purchasing the stock. The case of Claflin v. Farmers', etc., Bank, 25 N. Y. 293, has been cited as sustaining the contention of the railway company. But this case was distinguished from a case like the present one by the court delivering the opinion, as well as by the same court in the later case of Titus v. Great Western, etc., Co., 61 N. Y. 237. In the former case the president of a bank, having a general authority to certify checks upon it as good, certified one in his own favor. This the court held was out of the ordinary course of business, and contrary to business and legal rules, and not within the scope of the agency, but was particular to distinguish it from the issuing or transfer of a certificate of stock. The recent case of Knox v. Eden Musee, etc., Co., 148 N. Y. 441, 31 L. R. A. 779, needs to be noticed. In that case it will be observed that Jurgens, the wrongdoer, was not the agent of the company to issue or transfer stock. His employment was simply to cancel surrendered stock. Surrendered certificates were by him abstracted from the safe of the company and pledged as security for a loan. With respect to this the court said: 'If it can be said that the direction of the president to Jurgens to cancel the certificates made him the agent of the company for that purpose, it was an authority to destroy, and not use. His act in abstracting them from the safe and uttering them as valid certificates had no relation to the authority conferred. It was not an act of the same kind as that which he was authorized to perform. He had no apparent authority to issue them as genuine certificates, because he had no authority to issue certificates for any purpose.' This broadly distinguishes the case from the one before us. No disposition is shown to modify the doctrine of the same court as announced in many previous cases as to the liability of a corporation for the acts of its agents done within the scope of their employment, although not only negligently, but even fraudulently, done, and contrary to the purpose and instructions of the company. This clearly appears from the decision in Jarvis v. Manhattan, etc., Co., 148 N. Y. 652, 31 L. R. A. 776, decided at the same term. The case draws the distinction between negotiable instruments and certificates of stock. The former, though lost or stolen, are available in the hands of an innocent purchaser for value, whereas the latter are not."

the president and secretary under the seal of the company, and no other mode is provided or can be used, and neither the president nor the secretary is prohibited from holding stock, and both, with its knowledge, do in fact hold stock, the fact that a certificate is issued in favor of the secretary is not of itself sufficient to put a party on inquiry as to whether the secretary is rightfully the owner of it. By reason of what appears on the face of a certificate of stock, and the fact that, as a matter of general knowledge in the business world, such certificates of stock are extensively purchased as investments with no other inquiry than as to the genuineness of the signatures of the officers to the certificates, and that such use of them adds to the value of the stock of a company, and is largely to its advantage, the company is charged with the duty of observing care in their issue, and of supervising their agents charged with the performance of the duty. This is a duty it owes to all persons dealing in its stock, and if by reason of its negligence in this regard, spurious stock is issued, it is liable in damages to any one purchasing it for value without knowledge of its fraudulent character. The failure of a party under such circumstances to inquire at the office of the company is not such negligence as will deprive him of the right to recover, although such inquiry would have disclosed the fraudulent character of the certificates. The liability of the corporation under such circumstances is supported by the great weight of authority.[1] A corporation is liable to bona

[1] Western, etc., R. Co. v. Franklin Bank, 60 Md. 36; New York, etc., R. Co. v. Schuyler, 34 N. Y. 30; Bank of Kentucky v. Schuylkill Bank, 1 Pars. Eq. Cas. 180, affirmed on appeal by the supreme court; Hackensack, etc., Co. v. De Kay, 36 N. J. Eq. 548; Merchants' Bank v. State Bank, 10 Wall. 604, 19 L. ed. 1008; People's Bank v. Kurtz, 99 Pa. St. 344, 44 Am. Rep. 112; Titus v. Great Western Turnpike Road, 61 N. Y. 237; Bruff v. Mali, 36 N. Y. 200; McNeil v. Tenth Nat'l Bank, 46 N. Y. 325, 7 Am. Rep. 341; Moore v. Metropolitan Nat'l Bank, 55 N. Y. 41, 14 Am. Rep. 173; Holbrook v. New Jersey, etc., Co., 57 N. Y. 616; Bridgeport Bank v. New York, etc., R. Co., 30 Conn. 231; Tome v. Parkersburg, etc., R. Co., 39 Md. 36, 17 Am. Rep. 540; Willis v. Fry, 13 Phila. 33; First Nat'l Bank v. Lanier, 11 Wall. 369; Allen v. South Boston R. Co., 150 Mass. 200, 5 L. R. A. 716; Jarvis v. Manhattan, etc., Co., 148 N. Y. 652, 31 L. R. A. 776; Fifth Avenue Bank v. Forty-second Street, etc., R. Co., 137 N. Y. 231, 19 L. R. A. 331

fide holders of forged certificates regular on their face, but fraudulently issued by the secretary who was also the treasurer and transfer agent, and who countersigned them in his official capacity after forging the signature of the president.[1]

The title of the true owner of a lost or stolen stock certificate may be asserted even against one who subsequently acquires it in good faith for value.[2]

§ 325. **Liability to innocent purchasers only.**—The liability of the corporation to a holder of stock issued fraudulently or in excess of its power is to those only who acquire the stock without knowledge of its fraudulent character. There is no estoppel in favor of one who had knowledge of its invalidity, or of facts sufficient to put him upon inquiry.[3] A statement in the certificate received that no certificate can be lawfully issued without the surrender of the old certificate is sufficient to deprive the person receiving it of the status of an innocent purchaser. The certificate was issued by the cashier of a bank as security for his personal debt. The court said that none of the cases affirmed a broader doctrine than this. "A certificate of stock in a corporation, under the corporate seal and signed by the officer authorized to issue certificates, estops the corporation to deny its validity as against one who takes it for value, and with no knowledge or notice of any fact tending to show that it has been irregulary issued."[4] But the fact that a certificate of stock is issued in favor of the secretary of the corporation is not sufficient to put a purchaser upon in-

[1] Fifth Avenue Bank v. Forty-second Street, etc., R. Co., 137 N. Y. 231, 19 L. R. A. 331, annotated.

[2] Knox v. Eden, etc., Co., 148 N. Y. 441, 31 L. R. A. 779, § 450, *infra*. As to the liability of the company for making a transfer of shares upon the authority of a forged power of attorney, see § 452, and Pennsylvania Co. v. Franklin, etc., Co., 181 Pa. St. 40, 37 L. R. A. 780.

[3] Byers v. Rollis, 13 Colo. 22.

[4] Moores v. Citizens' Nat'l Bank, 111 U. S. 156. In Farrington v. South Boston, etc., Ry. Co., 150 Mass. 406, 15 Am. St. Rep. 222, it was held that the corporation was not estopped to deny the validity of stock certificates fraudulently issued by one of its officers to secure a private debt when the creditor knew that the surrender and transfer of the old certificate were prerequisites to the lawful issue of the new one and took no steps to see that this was done.

quiry as to whether he is rightfully the owner, where no other mode of issuing stock than by the president or the secretary under the corporate seal is provided, and neither the secretary nor the president is prohibited from holding stock.[1]

§ 326. **Recovery of money paid for void shares.**—The trustees of a corporation organized under the New York manufacturing act passed a resolution increasing its capital stock from $1,000,000 to $1,200,000, allowing each shareholder to take one share of the new stock for each five shares of the original stock which he held, and providing that on his paying $80 on each share of $100, a certificate for full paid stock should be issued to him by the company, and on his failure to pay an installment of $20 per share on or before a specified date, his claim to the new stock should be forfeited, and such forfeited shares divided ratably among the other stockholders who had paid that installment. A subscription agreement binding the subscribers thereto to take stock and pay $80 per share in installments as they should be called for by the company, and on failure to pay any installment to submit to the forfeiture of all sums theretofore paid, was signed by one of the trustees who had been active in the promotion of the scheme for the increase of the stock. He paid one installment of twenty per cent., and upon failure to pay another the stock was forfeited. The capital stock was afterwards reduced and bonds issued to refund the payments made on the new stock which was thus withdrawn. The trustee, whose stock had been forfeited, received none of the bonds and sued to recover the amount he had paid, and was allowed to recover on the ground that the contract remained executory, and although prohibited by law was not *malum in se*.[2] The plan to increase the stock was in violation of the law,[3] but the court adopted the rule as stated by Parsons: "'All contracts which provide that anything shall be done which is distinctly prohibited by law, or

[1] Cincinnati, etc., R. Co. v. Citizens' Nat'l Bank, 56 Ohio St. 351, 47 N. E. Rep. 249.

[2] Spring Co. v. Knowlton, 103 U. S. 49, but see Clark v. Lincoln, etc., Co., 59 Wis. 655; Potter v. Necedah, etc., Co. (Wis.), 80 N. W. Rep. 88.

[3] Knowlton v. Congress, etc., Co., 57 N. Y. 518; Parsons Contracts, vol. 2, p. 746.

morality, or public policy, are void, so he who advances money in consideration of a promise or undertaking to do such a thing may at any time before it is done rescind the contract and prevent the thing from being done and recover back his money.'''

§ 327. **Payment for stock.**—To the amount authorized by its charter a corporation may issue its stock in pursuance of a contract of subscription, and accept in payment therefor either cash, labor or property, taken at a reasonable valuation. While stock need not be paid for in cash, it must be paid for in the equivalent of cash.[1] The property accepted in payment must be at a fair and just valuation, fairly equivalent to what it is worth in money and equal to the par value of the stock.[2] Whatever may have been formerly held, it is now established that subscriptions to corporate stock need not, in the absence of statutory provisions requiring it, be paid for in cash. The principle is generally accepted, both in England and America, that any property which the corporation is authorized to purchase, or which is necessary for the purposes of its legitimate business, may be received in payment for its stock. Any payment, whether it be in money or money's worth, so that it be in good faith, will give the shares so paid for the status of paid-up stock.[3] In the language of Lord Justice Gifford in Drummond's case: If a man contracts

[1] Gamble v. Queens County, etc., Co., 123 N. Y. 91, 25 N. E. Rep. 201; Wetherbee v. Baker, 35 N. J. Eq. 501; Douglass v. Ireland, 73 N. Y. 100; Camden v. Stuart, 144 U. S. 104; Coit v. Amalgamating Co., 119 U. S. 343.

[2] Van Cleve v. Berkey, 143 Mo. 109, 44 S. W. Rep. 743. In Sprague v. National Bank of America, 172 Ill. 149, it was held that a transfer of all the assets of a corporation to a new company in consideration of its assuming the indebtedness of the old one and exchanging its stock, share for share, for that of the old company, thereby giving each shareholder the same relation to the property that he previously sustained, does not constitute a contract of bargain and sale of the assets, or establish that their value is sufficient to pay for the new stock in full. As against the creditors of the old company the stock will be considered as paid only to the extent of the actual value of the property received from the old company.

[3] Hayden v. Atlanta Cotton Factory, 61 Ga. 233; Richwald v. Commercial Hotel Co., 106 Ill. 439; Liebke v. Knapp, 79 Mo. 22; Coffin v. Ransdell, 110 Ind. 417; Carr v. Le Fevre, 27 Pa. St. 413; Brant v. Ehlen, 59 Md. 1.

to take shares he must pay for them, to use a homely phrase, in meal or in meat; he must either pay in money or money's worth.

IV. Watered Stock.

§ 328. **Meaning of the phrase.**—The adjective "watered" is used to describe stock which is issued as paid up but which has not in fact been paid up. The difference between the amount actually paid and the par or face value of the shares is said to be water. Such stock is issued by taking a partial cash payment, by accepting property at an overvaluation, or by the issue of an invalid stock dividend. The result in all cases is an over-capitalization. After such shares reach the hands of a bona fide transferee the holder is not liable to any greater extent than the holder of ordinary full-paid shares. But so long as they are in the hands of the original holders "the stock is liable to be canceled. The person to whom it was issued, or his transferee with notice, or the corporate officers participating in the act, may, under certain circumstances, each be held personally liable for the unpaid par value of the stock. They may be liable to the corporation itself, or to the corporate creditors, or to bona fide transferees of the stock."[1]

§ 329. **Issue of shares below par—The common law rule.**—The rule supported by the weight of authority in the United States is that, when not restricted by its charter or by a general law, a corporation may, if all the subscribers consent, legally issue its shares to subscribers under a contract by which they are to pay a less sum therefor than is represented by their face or par value. As between the subscriber and the corporation the question is purely one of contract, and if the corporation agrees to accept less than par for its shares it can not thereafter repudiate the contract and recover the difference from the stockholders.[2] There are some cases, however, which state the

[1] Cook Corp., § 32.

[2] Hebberd v. Southwestern, etc., Co., 55 N. J. Eq. 18, 36 Atl. Rep. 122; Scovill v. Thayer, 105 U. S. 143; Kenton, etc., Co. v. McAlpin, 5 Fed. Rep. 737; First Nat'l Bank v. Gustin, etc., Co., 42 Minn. 327; Arrapahoe, etc., Co. v. Stevens, 13 Colo. 534; Northern Trust Co. v. Columbia, etc., Co., 75 Fed. Rep. 936; Wells v. Green Bay, etc., Co., 90 Wis. 442; Lorillard v. Clyde, 86 N. Y. 384. But see Mor-

rule broadly that a corporation can not issue its shares for less than par,[1] but it is submitted that the accepted rule is otherwise. The English courts, under the present statute, hold, on the theory that such an issue is prejudicial to the rights of prior shareholders who have paid in full, that stock must be paid for at its full par value. A holder of full paid ordinary shares was allowed to force the purchaser of certain shares which were issued as full paid for sums less than their face, to pay the difference in order to create a fund which would be sufficient to pay off certain debentures which were charges against the entire property of the corporation. The result was to greatly increase the value of the ordinary shares.[2] Lord Chancellor Halsbury stated that the solution of the question was to be found in the nature of the contract of subscription, which is "an agreement to become liable to pay to the company the amount for which the shares have been created. That agreement is one which the company itself has no authority to alter or qualify, and I am therefore of opinion that the company were prohibited by law—from doing what is compendiously described as issuing shares at a discount." Lord Herschel, dissenting, said that, in his judgment, the company would not be entitled to call upon such shareholders for any further favors beyond that agreed upon, except in the case of the winding up, and then only so far as necessary for the discharge of the obligations of the company. In New York it was held that a contract between the corporation and the stockholder was valid even as against creditors, but this is not in accordance with the weight of authority.[3]

Stock which has been fraudulently issued as paid up, and

row v. Iron, etc., Co., 87 Tenn. 262; Winston v. Dorsett, etc., Co., 129 Ill. 64. 4 L. R. A. 507.

[1] See *dicta* in Barnes v. Brown, 80 N. Y. 527; Coleman v. Howe, 154 Ill. 458; Sturges v. Stetson, 1 Biss. (C. C.) 246; Oliphant v. Woodburn, etc., Co., 63 Iowa 332. It is often said to be an *ultra vires* act. Fisk v. Chicago, etc., R. Co., 53 Barb. (N. Y.) 513. But *ultra vires* acts are not always void.

[2] Ooregum, etc., Co. v. Roper (H. L.), 61 Law J. (N. S.) 337; Law Rep. App. Cases (1892), 125.

[3] Christesen v. Eno, 106 N. Y. 97.

which has not reached the hands of a bona fide holder, may, at the instance of a dissenting stockholder, be withdrawn and the certificates canceled.[1]

§ 330. **As between stockholder and creditor.**—Whether a certain issue of stock is valid or not will depend upon who complains of the issue. It may be valid as to the immediate parties to the issue, and invalid as to creditors of the corporation. After a corporation becomes insolvent its assets become a trust fund for the benefit of its creditors, and among such assets are included all unpaid subscriptions. The obligation of the stockholders to the creditors is considered as growing out of the *relation* and not of the contract between the corporation and the stockholders. The subscription agreement is construed as a contract to pay the company for the benefit of its creditors the amount for which the shares have been created and issued. This rule is based upon the principle of public policy which forbids a corporation as against its creditors to create stock for which it has not received in property or cash the full face value as represented by the shares. It may be considered as settled law that as against its creditors a corporation has no power in the first instance to issue its capital stock for less than its full par value. Hence, persons who purchase such shares *from the corporation* at less than their par value are, in the event of the insolvency of the corporation, liable to pay for the benefit of its creditors at least the difference between that which they have actually paid and the par value of the shares.[2] The issuance of the shares is treated as a representation to the public that the corporation has property equivalent to their face value. "It is so held out to the public who have no means of knowing the private contracts made between the corporation and its stockholders. The creditor has, therefore, the right to presume that the stock subscribed

[1] Gilman, etc., R. Co. v. Kelly, 77 Ill. 426. See Sturges v. Stetson, 1 Biss. 246.

[2] Hawley v. Upton, 102 U. S. 314; Upton v. Tribilcock, 91 U. S. 45; Sawyer v. Hoag, 17 Wall. U. S. 610; Camden v. Stuart, 144 U. S. 104; Alling v. Wenzel, 133 Ill. 264; First Nat'l Bank v. Gustin Minerva, etc., Co., 42 Minn. 327.

for has been or will be paid up, and if it is not, a court of equity will, at his instance, require it to be paid.'"[1] The same result is reached if we reject the trust fund theory and place the rule upon the ground of fraud.[2]

A distinction is made between the liability of subscribers to the original stock and those who receive stock subsequently issued and sold for its actual value in the market for the purpose of raising money necessary to carry on the business of the corporation and preserve it from ruin; but the subscribers to an increase of capital stock which is added to the original stock for the mere purpose of extending its business, and not to save it from wreck, are said to be liable in the same manner as the subscribers to the original stock.[3] The distinction, however, is somewhat difficult to perceive, and more difficult to properly apply.

§ 331. **Recital that shares shall be deemed fully paid up.**— An agreement between the shareholder and the corporation that the shares shall be deemed fully paid up is ineffectual as against the creditors.[4] But a purchaser or assignee of shares of stock in a corporation without notice that it has not been fully paid up does not become liable to the corporate creditors for the unpaid balance, where the stock was issued as fully paid up.[5] "Even in England, where the questions are generally considered solely with reference to the rights of the shareholders *inter se*,[6] such agreements, as between the original parties and their privies, have been declared invalid by the

[1] Scovill v. Thayer, 105 U. S. 143.

[2] Hospes v. Northwestern, etc., Co., 48 Minn. 174.

[3] Flinn v. Bagley, 7 Fed. Rep. 785. In Handley v. Stutz, 139 U. S. 417, the court said: "In the Upton cases arising out of the failure of the Great Western Insurance Company, in Hatch v. Dana, 101 U. S. 205, and in Hawkins v. Glenn, 131 U. S. 319, the defendants were either original subscribers to the increased stock at a price far below its par value, or transferees of said subscribers; and the stock was issued, not, as in this case, to purchase property or raise money to add to the plant and facilitate the operations of the company, but simply to increase its original stock in order to carry on a larger business, and the stock thus issued was treated as if it formed a part of the original capital."

[4] Wallace v. Carpenter, etc., Co., 70 Minn. 321, 73 N. W. Rep. 189.

[5] Sprague v. National Bank of America, 172 Ill. 149, 42 L. R. A. 606.

[6] Poole's Case, 9 Ch. Div. 322.

courts.[1] And even the supreme court of the United States concedes the principle, while refusing to apply it, that a contract between the subscribers to stock and the corporation, that the stock shall be considered as fully paid and non-assessable, or otherwise limiting their liability therefor, is void as against creditors.[2] And we may conclude with great confidence that the general doctrine is, except in so far as it has been shaken in California,[3] Minnesota,[4] New York,[5] and in the supreme court of the United States,[6] that any agreement, secret or otherwise, between the corporation and its shareholders that its shares shall not be paid in full, though possibly good as between the corporation and its shareholders, is void as to creditors of the corporation in the event of its insolvency." The foregoing is the very conservative statement of the law by Judge Thompson, who is very strongly opposed to the doctrine that a corporation can, under any circumstances, issue stock for less than par. The word "non-assessable" upon a stock certificate is merely a protection against further assessments after the par value of the stock has been paid.[7] All fictitious arrangements by which stock is issued as paid when not in fact paid are ineffectual. Thus an arrangement by which stock was nominally paid for in full and the money returned to the stockholder in the form of a loan was held ineffectual to protect the stockholder as against the creditors of the corporation.[8] One who receives stock as full paid but in fact as a gift, for the purpose of securing his influence on behalf of a corporation may be called on to pay for the stock after the corporation becomes insolvent.[9]

§ 332. **Bona fide purchasers of shares.**—A person who purchases stock with notice of the fact that it has not been fully paid up is liable thereon to the same extent as his transferrer.[10]

[1] Daniell's Case, 1 De J. J. 372.

[2] Handley v. Stutz, 139 U. S. 417.

[3] Stein v. Howard, 65 Cal. 616.

[4] Hospes v. Northwestern Car, etc., Co., 48 Minn. 174.

[5] Christensen v. Eno, 106 N. Y. 97, 60 Am. Rep. 431.

[6] Scovill v. Thayer, 105 U. S. 143, and other cases.

[7] Upton v. Tribilcock, 91 U. S. 45.

[8] Sawyer v. Hoag, 17 Wallace U. S. 610; Hays Case, L. R. 10 Ch. App. 593.

[9] Peninsular Savings Bank v. Black, etc., Co., 105 Mich. 535.

[10] Upton v. Tribilcock, 91 U. S. 45; Coleman v. Howe, 154 Ill. 458; Boul-

Although a recital in the certificate that the shares are fully paid is of no effect as between the creditors of the corporation after its insolvency and the original holders, the cases are in substantial accord upon the proposition that a bona fide purchaser of shares who relies upon the recital in the certificate is not liable to the corporate creditors because of the fact of their non-payment by the original holders.[1] In an action by a creditor against the holder of bonus or watered shares, the burden is on the holder to show that he acquired his shares bona fide without notice of the facts which make the issue fraudulent as to the creditor or that he purchased the stock from a bona fide innocent transferee.[2] Any subsequent transferee from a bona fide holder is protected.[3]

The ordinary form of stock certificate which contains nothing to show that the stock is not fully paid, and is silent as to whether it is fully paid or not, implies that it is fully paid, and a bona fide purchaser thereof is entitled to rely upon this presumption.[4] "Where shares are issued by the company to the subscriber as full paid shares, and are sold by the subscriber as such, there is no ground on which a promise can be implied, on the part of the purchaser without notice, to be answerable either to the company or its creditors. Should the representations on the faith of which he purchased prove to be false, he could not be held liable on the ground of contract, because he never agreed to purchase any other shares than

ton, etc., Co. v. Mills, 78 Iowa 460; White v. Greene (Iowa), 70 N. W. Rep. 182.

[1] Webster v. Upton, 91 U. S. 65; Protective, etc., Co. v. Osgood, 93 Ill. 69; Young v. Erie, etc., Co., 65 Mich. 111; Brant v. Ehlen, 59 Md. 1; Steacy v. Little Rock, etc., R. Co., 5 Dill. (C. C.) 348. *Contra*, Tasker v. Wallace, 6 Daly (N. Y.) 364; Foreman v. Bigelow, 4 Cliff. (C. C.) 508; Troup v. Horbach (Neb.), 74 N. W. Rep. 326. For the English rule, see Re Concession Trust (1896), 2 Ch. 757.

[2] Wallace v. Carpenter, etc., Co. (Minn.), 73. N. W. Rep. 189.

[3] Barrow's case, L. R. 14 Ch. Div. 432.

[4] Young v. Erie, etc., Co., 65 Mich. 111; West Nashville Planing Mill v. Nashville Sav. Bank, 86 Tenn. 252; Johnson v. Lullman, 15 Mo. App. 55; Albitztigui v. Guadalupe, etc., Co., 92 Tenn. 598; Rood v. Whorton, 67 Fed. Rep. 434, 74 Fed. Rep. 118; Coleman v. Howe, 154 Ill. 458; Steacy v. Little Rock, etc., R. Co., 5 Dill. (C. C.) 348; Keystone, etc., Co. v. McCluney, 8 Mo. App. 496.

full paid shares; and if it be said that the shares were fraudulently issued, he could not be held liable on the ground of fraud, because he was in no sense a party to the fraud.'"[1] But the mere fact that stock is marked "non-assessable" does not protect a transferee from liability for unpaid calls, as these words are not construed to refer to calls or assessments necessary to make stock full paid.[2] So the statement that the stock is full paid will not protect against assessments provided for by the charter.[3] Statements of officers and directors that stock is full paid unless shown to have been made in the performance of their duties can not be relied upon by a purchaser and are not sufficient to make him a bona fide holder of the stock without notice.[4]

§ 333. **Who may complain.**—The issue of watered stock is an *ultra vires* act on the part of the corporation, and if it appears that the issue of the shares will result in defrauding the public, the state may, in a proper proceeding, have the corporate charter forfeited.[5] It has been held that *quo warranto* will not lie against a corporation merely because of the issue of stock below par.[6] The corporation is estopped to deny the contract to accept less than par for its stock. So, stockholders who participate or aid in the issue of the stock or who acquiesce therein can not afterwards be heard to complain.[7] A transferee of a participating stockholder can not complain of the transaction, as his remedy is against those who induced him to purchase the stock.[8]

[1] Brant v. Ehlen, 59 Md. 1.

[2] Webster v. Upton, 91 U. S. 65; Upton v. Tribilcock, 91 U. S. 45.

[3] Western, etc., Co. v. Des Moines Nat'l Bank (Iowa), 72 N. W. Rep. 657.

[4] Browing v. Hinkle, 48 Minn. 541; Webster v. Upton, 91 U. S. 65.

[5] State v. Webb, 97 Ala. 111; State v. Janesville, etc., Co., 92 Wis. 496; Cheetham v. McCormick, 178 Pa. St. 186.

[6] State v. Minnesota, etc., Co., 40 Minn. 213.

[7] TenEyck v. Pontiac, etc., R. Co. (Mich.), 72 N. W. Rep. 362; Woolfolk v. January, 131 Mo. 620; Washburn v. National, etc., Co., 81 Fed. Rep. 17; Clark v. American, etc., Co., 86 Iowa 436.

[8] Higgins v. Lansingh (Ill.), 40 N E. Rep. 362; Barr v. New York, etc. Co., 125 N. Y. 263; Church v. Citizens', etc., R. Co., 78 Fed. Rep. 526.

§ 334. **Liability is to subsequent creditors only.**—Only those who become creditors of the corporation after the issue of the fictitious or part paid stock can be heard to object, as they only can possibly be injured by the transaction.[1] In First National Bank v. Guston, etc., Co., *supra*, the court says: "It is only those creditors who can fairly allege that they have relied, or whom the law presumes to have relied, upon the amount of capital stock of the company who have a right to make such inquiry or in whose favor equity will impress a trust upon the subscription to the stock and set aside a fictitious arrangement for its payment. For example, to distribute the capital among the stockholders without provision for paying corporate debts would be a fraud on existing creditors as well as on subsequent creditors who dealt with the corporation, in reliance upon the assumption that its professed capital remains intact." The court further said that there were no cases "where any such trust has been enforced in favor of creditors who have dealt with the corporation with full knowledge of the facts. The reason is apparent, for in such cases no fraud, actual or constructive, has been committed on such creditors. If a corporation issues new shares after the claim of a creditor arose, it is clear that the latter could not have dealt with the company on the faith of any capital represented by them. Whatever was contributed as capital in respect of the new shares was a clear gain to the creditor's security. So, too, if a party deals with a corporation, with full knowledge of the fact that its nominal paid-up capital has not, in fact, been paid for in money or property to the full amount of its par value, he deals solely on the faith of what has been actually paid in and

[1] Handley v. Stutz, 139 U. S. 417; Coit v. Gold, etc., Co., 119 U. S. 343, 14 Fed. Rep. 12; Hospes v. Northwestern, etc., Co., 48 Minn. 174, 15 L. R. A. 470; First Nat'l Bank v. Gustin, etc., Co., 42 Minn. 327, 6 L. R. A. 676; Dummer v. Smedley, 110 Mich. 466, 38 L. R. A. 490. The original holders of bonus or watered stock of a corporation issued as paid-up, and their transferees with notice, will, in case of the insolvency of the corporation, be charged, in favor of the creditor who become such after the stock was issued, with the difference between the par value of the stock and the amount paid the corporation therefor, to the extent necessary to pay the creditor's claims. Wallace v. Carpenter, etc., Co. (Minn.), 73 N. W. Rep. 189; Hastings, etc. Co. v. Iron, etc., Co., 65 Minn. 28.

has no equitable right to insist on the contribution of a greater amount of capital by the shareholders than the corporation itself could claim as part of its assets.'"[1]

§ 335. **Bonus stock given to "sweeten" bonds.**—The issue of purely gratuitous or bonus stock is universally condemned, and either held void or payment therefor required from its holders in favor of corporate creditors. In some cases, however, it is held that the issue of stock to the purchasers of bonds of a corporation, to induce them to purchase the securities, is valid, even as against subsequent creditors. When the issue of shares for less than par is permitted as between the corporation and the taker, it is clear that one who was a creditor of the corporation before such issue can not attack the transaction, as even on the trust fund theory the trust does not attach until insolvency, and only those creditors who have at least presumptively become such on the security of the stock subscription can complain.[2] In a well known case[3] the actual value of the stock which was given to the purchasers of the bonds in equal amounts, in order to induce them to purchase the bonds, added to the actual value of the bonds, was not more than the par value of the bonds and the transaction was sustained. The cases which permit such transactions require that the corporation shall receive some fair and reasonable equivalent for the stock and the bonds.[4] In other jurisdictions the holders of such stock are held liable to the creditors for the full face value of the stock, on the ground that the transaction is a fraud on the creditors of the corporation.[5] In one

[1] First Nat'l Bank v. Gustin, etc., Co., 42 Minn. 327, 6 L. R. A. 676. In Richardson's Exrs. v. Green, 133 U. S. 30, it appeared that Richardson had advanced money on bonds and taken stock as a bonus. On a suit to foreclose the mortgage the moneys actually advanced by him were allowed, without any reduction on account of the bonus stock, though there were general creditors subsequent to the mortgage securing his bonds.

[2] See cases cited in preceding section.

[3] Handley v. Stutz, 139 U. S. 417. See, also, Brown v. Duluth, etc., R. Co., 53 Fed. Rep. 889, under statute: Richardson's Exrs. v. Green, 133 U. S. 31.

[4] Fogg v. Blair, 139 U. S. 118.

[5] Hebbard v. S. W. Land, etc., Co., 55 N. J. E. 18, 36 Atl. Rep. 122; Skrainka v. Allen, 7 Mo. App. 434, 76 Mo. 384; § 345.

case an agreement by which a subscriber to the original organization stock of the corporation, on payment therefor, was to have in addition to the stock an equal amount of the bonds of the company, was held invalid as a mere device to escape the obligation created by his subscription.[1]

§ 336. **Construction bonds and bonus shares.**—Railroad companies often issue bonds and stock to contractors in payment for material and services in the construction of the road in an amount at par much in excess of the actual value of the material or services, and such contracts have received judicial sanction.[2] But where a company made a construction contract under which the contractor agreed to furnish all the materials and do all the work necessary to construct the railroad at an expenditure not to exceed $200,000, and in consideration to receive $300,000 of the capital stock full paid, and the same amount of its first mortgage bonds, the contract was held invalid. The state constitution provided that "no corporation shall issue stocks or bonds except for money, labor done, or money or property actually received; and all fictitious increase of stock or indebtedness shall be void." And the court said: "The above quoted section of the new constitution has strangely miscarried if such an issue of watered stock and unsubstantial bonds can be emitted."[3]

The contractor had entered upon the work and expended considerable money, and although the contract was rescinded, compensation upon equitable terms was allowed for what had been done.

In another case it was held that a statute which prohibited any railroad company from selling or disposing of its stock unless such shares have been fully paid up, or issuing any bonds or stocks except for money, labor or property received and applied for the purpose for which the corporation was created,[4] does not forbid the issue of first-mortgage bonds and

[1] Morrow v. Nashville, etc., Co., 87 Tenn. 262, 3 L. R. A. 37.

[2] Van Cott v. Van Brunt, 82 N. Y. 535.

[3] New Castle, etc., R. Co. v. Simpson, 21 Fed. Rep. 533.

[4] Laws Minn., 1887, ch. 12, § 1.

full paid stock by a railroad company in payment for the construction of its road, if the amount issued does not unreasonably exceed the value received. "This statute was not intended to prevent or interfere with the usual method of raising money to build railroads, or for any legitimate corporate purpose. It is not to be construed as obstructive to the extent of restricting or hampering corporations in their internal management, and embarrass them in procuring means to carry out the legitimate purposes of the corporation; and unless it appears that, under the guise of building its road, bonds and stocks of the defendant company are to be issued and put upon the market fraudulently, that do not and are not intended to represent money or property, this corporation is not prohibited from entering into a real transaction based upon a present consideration and having reference to legitimate corporate purposes."[1]

§ 337. **Stock issued by a going concern with impaired capital.**—A distinction is sometimes made between an original subscription for stock and a sale of stock. The principle is recognized in cases cited in the preceding section. The supreme court of the United States has established the doctrine that a going corporation which requires money for the purpose of carrying on its business may issue its bonds and stock and sell the same together for what they are actually worth in the market. In the leading case it appeared that the corporation found its original capital impaired, and for the purpose of raising capital with which to preserve itself by extending its business into new and more promising fields, issued bonds secured by mortgage upon its property. In order to effect a sale of these bonds new stock was issued to the purchasers of the bonds dollar for dollar. Thus each purchaser of a thousand-dollar bond received in addition to the bond, a thousand dollars face value of stock, "full paid and non-assessable." The court, by Brown, J., said: "The case then resolves itself into the question whether an

[1] Brown v. Duluth, etc., R. Co., 53 Dow, 120 U. S. 287. Fed. Rep. 889, citing Railroad Co. v.

active corporation, or as it is called in some cases 'a going concern,' finding the original capital impaired by loss or misfortune, may not, for the purpose of recuperating itself and providing new conditions for the successful prosecution of its business, issue new stock, put it upon the market and sell it for the best price that can be obtained. The question has never been directly raised before in this court, and we are not, consequently, embarrassed by any previous decisions on the point. * * * To say that a corporation may not, under the circumstances above indicated, put its stock upon the market and sell it to the highest bidder, is practically to declare that a corporation can never increase its capital by a sale of shares, if the original stock has fallen below par. The wholesome doctrine, so many times enforced by this court, that the capital stock of an insolvent corporation is a trust fund for the payment of its debts, rests upon the idea that the creditors have a right to rely upon the fact that the subscribers to such stock have put into the treasury of the corporation, in some form, the amount represented by it; but it does not follow that every creditor has the right to trace each share of stock issued by such corporation, and inquire whether the holder, or the person of whom he purchased, has paid the par value for it. It frequently happens that corporations, as well as individuals, find it necessary to increase their capital in order to raise money to prosecute their business successfully, and one of the most frequent methods resorted to is that of issuing new shares of stock and putting them upon the market for the best price that can be obtained; and so long as the transaction is bona fide, and not a mere cover for 'watering' the stock, and the consideration obtained represents the actual value of such stock, the courts have shown no disposition to disturb it. Of course no one would take stock so issued at a greater price than the original stock could be purchased for, and hence the ability to negotiate the stock and to raise the money must depend upon the fact whether the purchaser shall or shall not be called upon to respond for its par value. While, as before observed, the precise question has never been raised in this court, there

are numerous decisions to the effect that the general rule that holders of stock, in favor of creditors, must respond for its par value, is subject to exceptions where the transaction is not a mere cover for an illegal increase.[1] * * * We think that an active corporation may, for the purpose of paying its debts, and obtaining money for the successful prosecution of its business, issue its stock and dispose of it for the best price that can be obtained.'"[2] On the same principle it has been held that a corporation may issue stock at its actual market value and take payment therefor in property or services of which it is in need. Thus, a railroad company in good faith made a contract for the construction of its road and agreed to pay therefor in its stock at its actual instead of par valuation, and it was held that the holders of the stock were not liable to the creditors of the corporation.[3]

§ 338. **Shares accepted as a gratuity.**—It is held in New York that no liability attaches to one who accepts unpaid shares as a mere gratuity. The liability is made to rest entirely on the contract of subscription, and as in such case there is no contract between the holder and the corporation the creditors have no basis for a claim upon him for the nominal value of the shares.[4] This rule is in conflict with the cases which hold that subsequent creditors are allowed to call upon the stockholders and is not in accord with the weight of authority. In general no distinction is made between the liability of one who is a subscriber for such stock and one who receives it merely as a gift.[5]

[1] See Harrison v. Arkansas, etc., R. Co., 4 McCrary 264; Van Cott v. Van Brunt, 82 N. Y. 535; Stein v. Howard, 65 Cal. 616; Dummer v. Smedley, 110 Mich. 466, 68 N. W. Rep. 260. See Clark v. Bever, 139 U. S. 96; Morrow v. Iron Co., 87 Tenn. 262; Rickerson, etc., Co. v. Farrell, etc., Co., 75 Fed. Rep. 554; Peters v. Union, etc., Co. (Ohio), 46 N. E. Rep. 894. *Contra*, Jackson v. Traer, 64 Iowa 469, 20 N. W. Rep. 764.

[2] Handley v. Stutz, 139 U. S. 417.

[3] Van Cott v. Van Brunt, 82 N. Y. 535; Barr v. Railroad Co., 125 N. Y. 263.

[4] Christensen v. Eno, 106 N. Y. 97, 60 Am. Rep. 429; Christensen v. Quintard, 8 N. Y. Supp. 400; Seymour v. Sturgess, 26 N. Y. 134.

[5] Peninsular Savings Bank v. Black, etc., Co., 105 Mich. 535.

§ 339. **Illustrations.**—The books are full of cases illustrating the principles stated in the preceding sections. Where a railway company was indebted to a construction company in the sum of $70,000, which it was unable to pay, and issued therefor stock of the par value of $350,000, the holders were treated as stockholders who had paid twenty per cent. on their stock.[1] Where $300,000 of stock was issued for property worth $68,000, the stockholders were held liable for the difference.[2] In this case the court said: "A deliberate and advised overvaluation of property thus purchased and paid for is a fraud upon the law, and a violation of the condition upon which the exemption of stockholders from liability under the provisions of the statute is made to depend. It is in direct violation of the policy as well as the terms of the law which demands payment either in money or property at its value, of all the capital stock of the company as a condition of immunity to the stockholders from liability for debts of the corporation. The payment of an amount for property in excess of its value deprives creditors and the public of the security contemplated by the statute, and thus a fraud is perpetrated as well upon the law as upon the creditors. * * * All that is necessary to establish legal fraud is to prove two facts: (1) That the stock issued exceeded the value of the property in exchange for which it was issued, and (2) That the trustees deliberately and with knowledge of the real value of the property overvalued it and paid in stock for it an amount which they knew was in excess of its actual value."[3]

Under a statute which authorized payment for corporate stock to be made "either in money or in land, the land to be appraised by the board of directors and taken at such value on such terms as may be agreed upon," $100,000 worth of stock was issued and subscribed for by five persons who

[1] Jackson v. Traer, 64 Iowa 469; Osgood v. King, 42 Iowa 478. The supreme court of the United States, in Clark v. Bever, 139 U. S. 96, refused to follow the decision in Jackson v. Traer, *supra*.

[2] Douglas v. Ireland, 73 N. Y. 100.

[3] To the same effect is Boynton v. Andrews, 63 N. Y. 93; Schenck v. Andrews, 57 N. Y. 133; Iron Company v. Drexel, 90 N. Y. 87.

afterward became the directors of the corporation. Certain lands worth $50,000 were purchased for that sum and the deed thereof made directly to the corporation, which gave its obligation for the whole amount. The directors then appraised the land at $100,000 and credited $50,000 of it as a payment of fifty per cent. on the stock subscribed for by them. The allowance of the credit on the stock was as against the creditors of the corporation held invalid, and the stockholders were required to pay the whole amount of their subscription. The court said:[1] "This appraisement, it is manifest, was illusory and made only in the interest of the directors who were to profit by it." Where a statute provided that "no share shall be issued for less than its par value," it was held, although the rights of the creditors were not involved, that where land was purchased for $125,000 on September 29th, and on October following the corporation agreed to take it at an advance of $50,000, so that a stock subscription of that amount made by the vendors should be thereby fully paid, the stock was not thereby paid. The transaction was regarded as a fraud on the other stockholders who had paid for their stock, and as not being in compliance with statutory safeguards intended for the protection of the public.[2] A shareholder in a water company, at an expense of $85,000, constructed a system of pipes suitable for the extension of the company's plant, and afterward sold it to the corporation for $110,000, payable in stock. The transaction was upheld on the ground that the difference was not so great as to show fraud.[3] The promoters of a corporation acquired a bond for a deed to certain real estate in the sum of $53,000. Thereafter they organized a corporation and issued $200,000 of stock, which was given to the promoters for a transfer of the bond for title. The real estate was found to be worth only $53,000 and the stockholders were held liable to the creditors for the difference.[4] One who received stock as paid up as considera-

[1] Wetherbee v. Baker, 35 N. J. Eq. 501.

[2] Bailey v. Coke Co., 69 Pa. St. 334.

[3] Gamble v. Queen's County, etc., Co., 123 N. Y. 91, 25 N. E. Rep. 201.

[4] Elyton, etc., Co. v. Birmingham, etc., Co., 92 Ala. 407, 12 L. R. A. 307.

tion for using his influence to sell the products of the corporation must pay the full par value of the stock to the corporate creditors.[1]

§ 340. **Payment in property.**—In many states there are statutes which provide that stock must be paid for in money or in property taken at its actual valuation. In the absence of such a statute, while a corporation may accept something other than cash in payment for its stock, it must be taken at a fair and equivalent valuation. The valuation to be considered is the value to the corporation and not the parties who sold it to the corporation.[2] The presumption is that the valuation at which property or services was taken by the corporation was adequate.[3] The fact that the actual value of the property proved much less than it was taken at is immaterial if the valuation was fair and honest at the time.[4] If stock is paid for in property or services at a gross overvaluation, and the corporation thereafter becomes insolvent, its creditors may, according to some authorities, require the holders of the stock to pay the difference between the actual value of the property and the par value of the stock; while other cases hold that, at least where there was actual fraud, the entire transaction is void and the holder is liable for the full value of the stock without a credit of the actual value of the property.[5] Before a creditor can require the holders of such stock to pay anything further, it must be shown that there was actual fraud or such gross overvaluation as to be the equivalent of fraud in law. Such a transaction may "be impeached for fraud but not for error of judgment or mistaken views of the value of property, inasmuch as good faith and the exercise of an honest judg-

[1] Peninsular Sav. Bank v. Black, etc., Co., 105 Mich. 535.

[2] Gamble v. Queen's County Water Co., 123 N. Y. 91, 9 L. R. A. 527. Distinguishing Van Cott v. Van Brunt, 82 N. Y. 535. See Gogebic Invest. Co. v. Iron Chief, etc., Co., 78 Wis. 426; In re Western, etc., Co., L. R. 1 Ch. Div. 115.

[3] Davis Bros. v. Montgomery, etc., Co., 101 Ala. 127, 8 So. Rep. 496.

[4] Coit v. Gold, etc., Co., 119 U. S. 343; Carr v. Le Fevre, 27 Pa. St. 413.

[5] See § 345, *infra*. Smith v. Prior, 58 Minn. 247. This case turns upon a question of pleading.

ment is all that is required."[1] In one case[2] it was said that "where full paid stock is issued for property received, there must be actual fraud in the transaction, to enable the creditors of a corporation to call the stockholders to account. A gross and obvious overvaluation of property would be strong evidence of fraud." This question was elaborately discussed in two recent cases. In the Montana case[3] it was held that good faith in the valuation of the property is all that the law demands. A Missouri case,[4] on the other hand, adopts an extreme position and holds that the property accepted in payment must be *in fact a fair equivalent* for the money subscribed, and that the belief of the stockholder that the property was equal in value to the par value of the stock will not relieve him from liability on his subscription as against those who have given credit to the company on the faith of its capital stock, if in fact the property is not of such value.

It is safe to say that the taking of property at a gross overvaluation is invalid without reference to the question of actual fraudulent intent, or, if the actual fraudulent intent is necessary, a gross overvaluation is sufficient evidence of its existence. Thus, where property worth $5,000 was taken to pay a stock subscription of $200,000, the court said that the transaction did not "bear the semblance of compliance with the contract of subscription as to one of the essential terms thereof. The taking of property at a valuation forty times greater than its actual worth, which was known to the parties, shows upon its face the absence of a bona fide exercise of judgment and discretion in making the valuation and an intentional noncompliance with the requirement that the property shall be

[1] Douglass v. Ireland, 73 N. Y. 100.

[2] Coit v. Gold, etc., Co., 119 U. S. 343; Bank v. Alden, 129 U. S. 372; Gamble v. Queen's County Water Co., 123 N. Y. 91, 25 N. E. Rep. 201; Young v. Iron Co., 65 Mich. 111; Whitehill v. Jacobs, 75 Wis. 474; Coffin v. Ransdell, 110 Ind. 417; Bickley v. Schlag, 45 N. J. Eq. 533; Clayton v. Ore Knob Co., 109 N. C. 385.

[3] Kelly v. Fourth of July, etc., Co., (Mont.), 53 Pac. Rep. 959, 42 L. R. A. 621. See also National Bank v. I. & W. L. Co., 101 Wis. 247; Northwestern, etc., Ins. Co. v. Cotton, etc., Co., 70 Fed. Rep. 155; Du Pont v. Tilden, 42 Fed. Rep. 87.

[4] Van Cleve v. Berkey (Mo.), 44 S. W. Rep. 743, 42 L. R. A. 593.

taken at its money value. The absence of fraudulent motive on the part of the trustee does not give validity to a mere simulated execution of the trust, and an averment of fraud in reference thereto is unnecessary. The parties beneficially interested in the trust are entitled to a substantial compliance with its terms. They are not bound by an act of mere formal compliance which really involved their practical exclusion from the benefits intended to be secured to them.'"[1] The allegation in a bill seeking to require the payment of the difference between the par value of shares and the actual value of property conveyed to the corporation, that all of the capital stock of $1,250,000 was paid for by a conveyance of real estate worth $100,000 is a sufficient allegation of fraud.[2]

§ 341. **Remedy where there is overvaluation.**—Where the stock is issued at a discount for cash, the stockholder, if liable at all, is liable for the difference between the amount paid and the par value of the shares. So it will be seen that in some cases it is held that, when property is taken in payment of stock at a gross overvaluation, the stockholder is liable to the corporate creditors for the difference between the actual value of the property at the time and the face or par value of the stock.[3]

[1] Elyton, etc., Co. v. Birmingham, etc., Co., 92 Ala. 407, 12 L. R. A. 307. Reviewing more cases.

[2] Lea v. Iron, etc., Co. (Ala.), 24 So. Rep. 28.

[3] Gates v. Tippecanoe, etc., Co., 75 Ohio St. 60, 63 Am. St. Rep. 705; Wishard v. Hansen, 99 Iowa 307, 61 Am. St. Rep. 238; Coleman v. Howe, 154 Ill. 458, 45 Am. St. Rep. 133; Cole v. Adams (Tex.), 49 S. W. Rep. 1052; Roman v. Dimmick, 115 Ala. 233; Hastings, etc., Co. v. Iron Range, etc., Co., 65 Minn. 28; Wallace v. Carpenter, etc., Co. (Minn.), 73 N. W. Rep. 189; Elyton, etc., Co. v. Birmingham, etc., Co., 92 Ala. 407 and cases there cited. See, aslo, Clayton, etc., Co. v. Ore Knob Co., 109 N. C. 385. In Elyton, etc., Co. v. Birmingham, etc., Co., 92 Ala. 407, 12 L. R. A. 307, the court said: "Our examination satisfies us that the weight of American authority does not support the statement made by Mr. Cook in section 46 of his work on Stock and Stockholders, to the effect that the attempts which have been made in cases where stock was issued for property taken at an overvaluation to hold the party receiving such stock liable for its full value less the actual value of the property received from him have been unsuccessful; and that if there has been an overvaluation which is shown to have been fraudulent, then the contract is to be treated

But the decisions are conflicting. It has been held that where it is alleged that a subscription is unpaid, it can not be shown that, although the property given was greatly overvalued, it nevertheless had some value, and that the stockholders should have credit for that amount. Where there is a fraudulent overvaluation of the property or services the entire transaction is generally held to be void, and the stockholders are liable to the creditors of the corporation for the full nominal value of the stock.[1] "During the past ten years," says Mr. Cook,[2] "there has been a vast amount of litigation on this subject. The courts still disagree in their conclusions, but a careful study of the cases will show that, upon authority as well as principle, the stockholders can not be held liable in such a case. In England and New York they can not be held liable at all, except on the basis of a rescission, and under all the well-considered decisions they can not be held liable unless the property is of so trifling a character that it practically has no value whatever. This class of cases has arisen under two aspects—first, at common law; and second, under statutes. At common law it is well settled that corporate creditors can not hold stockholders liable on stock which has been issued for property, even though the property was turned over to the corporation at an agreed valuation which was largely in excess of the real value of the property. There have been cases which refuse to follow this rule, but it is clearly established by the great weight of authority. The reason of the rule is, that if

like other fraudulent contracts and is to be adopted *in toto* or rescinded *in toto* and set aside."

[1] Smith v. Prior, 58 Minn. 247, 59 N. W. Rep. 1016; Peck v. Coalfield, etc., Co., 11 Ill. App. 88; Scovill v. Thayer, 105 U. S. 143. In Clayton v. Ore Knob Co., 109 N. C. 385, it appeared that there was a fraudulent overvaluation of the property, but the stockholder was given credit for the actual value of the property.

[2] Corporations, § 46. As supporting the rule that the stockholder can not be held liable unless there was fraudulent overvaluation of the property and a rescission on the contract, see Phelan v. Hazard, 5 Dill. (C. C.) 45; Van Cott v. Van Brunt, 82 N. Y. 535; Barr v. New York, etc., R. Co., 125 N. Y. 263; Seymour v. Spring Forest, etc., Assn., 144 N. Y. 333; Flynn v. Brooklyn, etc., R. Co., 9 N. Y. App. Div. 269; Coffin v. Ransdell, 110 Ind. 417; Bruner v. Brown, 139 Ind. 600; Bickley v. Schlag, 46 N. J. Eq. 533; Medler v. Albuquerque, etc., Co., 6 N. Mex. 331.

the payment by property was fraudulent, then the contract is to be treated like other fraudulent contracts. It is to be adopted *in toto* or rescinded *in toto* and set aside. Both parties are to be restored, as nearly as possible, to their original positions. The property, or its value, is to be returned to the person receiving the stock, and he must return the stock, or its value. In New York and England, as stated above, at common law, the stockholder is not liable at all to corporate creditors, even though the overvaluation was gross, and clearly shown so to be. The remedy is by rescission, and not the making of a new contract by the court. There are other cases, however, which hold that when the property so turned over has no substantial value, or where the valuation was 'fraudulent,' the court will hold the stockholders liable for the par value of the stock less the value of the property."

If the property given in payment for the stock has no value whatever there is no payment and the stockholder is liable on the stock. Thus, in one case, the court said: "The experience and good-will of the partners, which, it is claimed, were transferred to the corporation, are of too unsubstantial and shadowy a nature to be capable of pecuniary estimation in this connection."[1] Where the owner of a railroad sold it to a new organization and received in payment stock and bonds of the par value of fifty times the actual value of the railroad, it was held that the subscription price had never been paid. The court said: "The entire organization was grossly fraudulent from first to last, without a single honest incident or redeeming feature. It having been found on convincing evidence that the overvaluation of the property transferred to the railway company by Harper, in pretended payment of the subscriptions to the capital stock, was so gross and obvious as, in connection with the other facts in the case, to clearly establish a case of fraud, and to entitle bona fide creditors to enforce actual payment by the subscribers, it only remains to consider the effect of the defenses set up."[2]

The remedy of the corporate creditor is in equity and not at

[1] Camden v. Stewart, 144 U. S. 104. [2] Lloyd v. Preston, 146 U. S. 630.

law for fraud and deceit.[1] The bill may be for one on behalf of all.[2]

§ 342. **Constitutional and statutory provisions as to payment of shares.**—Many states have attempted to prevent the issue of watered stock by the adoption of statutory or constitutional provisions prohibiting corporations from issuing stock unless they receive a full equivalent therefor in money or property.[3] Care must be taken to distinguish between cases decided under these statutes and those on the common law.[4] The provision of the Illinois constitution, which refers, however, only to railroad corporations, is a fair illustration of all this class of prohibitions. It provides that "no railroad shall issue any stock or bonds, except for money, labor or property actually received and applied to the purposes for which said corporation was created, and all stock dividends and other fictitious increases of the capital stock or indebtedness of any such corporation shall be void." These provisions, however, are not, as a rule, given the sweeping effect which their language would seem to justify. The results of attempts to apply a remedy which makes the stock void after the mischief is done must fall heavily and unjustly upon innocent holders of stock. "The trouble with these constitutional prohibitions is that they attempt to cure the evil after the harm has been done instead

[1] Priest v. White, 89 Mo. 609; Coleman v. Howe, 154 Ill. 458.

[2] Cleveland, etc., Co. v. Texas, etc., R. Co., 27 Fed. Rep. 250.

[3] As to the difficulties in the way of applying these provisions, see State v. Webb, 110 Ala. 214; Van Cleve v. Berkey, 143 Mo. 109, 44 S. W. Rep. 743, 42 L. R. A. 593. See the constitutions of Alabama, art. 9, § 6; Arkansas, art. 12, § 8; California, art. 12, § 11; Colorado, art. 15, § 9; Idaho, art. 8, § 9; Illinois, art. 12, § 13; Kentucky, § 193; Louisiana, art. 238; Mississippi, § 196; Missouri, art. 12, § 8; Montana, art. 15, § 10; Nebraska, art. 11, § 5; North Dakota, § 138; Pennsylvania, art. 16, § 7; South Dakota, art. 17, § 8; Texas, art. 12, § 6; Washington, art. 12, § 6; Ohio (R. S., § 3313); Maine (Libby v. Tobey, 82 Maine 397); Wisconsin, Mowry v. Farmers', etc., Co., 76 Fed. Rep. 38; Minnesota (Gen. Stat. 1894, § 3415, Hastings, etc., Co. v. Iron, etc., Co., 65 Minn. 28; Wallace v. Carpenter, etc., Co., 73 N.W. Rep. 189); Tennessee (Jones v. Whitworth, 94 Tenn. 602); New Jersey (Baker v. Guarantee, etc., Co. (N. J.), 31 Atl. Rep. 174), and Iowa (Jackson v. Traer, 64 Iowa 469), have statutes to the same effect.

[4] See Railway. Co. v. Allerton, 18 Wallace U. S. 233.

of attempting to oversee the issue of stock and bonds before the issue is made." In Massachusetts the problem has been solved by a statute which prohibits the issue of stock or bonds for property until approved by state commissioners. The Minnesota statute prevents the issue of shares below par, with an exception which provides for special and preferred shares.[1]

[1] Wallace v. Carpenter Elec. Heating, etc., Co. (Minn.), 73 N. W. Rep. 189; Hastings, etc., Co. v. Iron, etc., Co., 65 Minn. 28; Gen. St. Minn. 1894, § 3415, provides: "Corporations having capital stock divided into shares, unless specially authorized, shall not issue any shares for a less amount to be actually paid in on each share than the par value of the shares first issued; provided, that railroad and navigation and manufacturing corporations, and corporations for buying, holding, improving, selling and dealing in lands, tenements hereditaments, real, mixed and personal estate and property, created or organized under this chapter, or under any charter or special act of incorporation heretofore passed, shall have power to create, issue and dispose of such an amount of special, preferred or full-paid stock of the capital stock of such corporation as may be deemed advisable by the board of directors of such corporation; provided, that any corporation may, by its articles of incorporation or by any amended article of its articles of incorporation, provide for special, preferred and common stock, or special or preferred and common stock, of the capital stock of such corporation; and any corporation heretofore or hereafter organized without changing its articles of incorporation may issue its capital stock as a part special and a part preferred and a part common, or a part common and a part either special or preferred, by direction of its board of directors, when so authorized by a majority of its stockholders at its annual meeting or at a meeting called for that purpose; and said board of directors, when so authorized by said meeting of said stockholders, may give such preference as it may deem best to such special or preferred stock, or such special and preferred stock."

This statute was held to apply to manufacturing as well as to other corporations. Wallace v. Carpenter, etc., Co., *supra*. Chief Justice Start said: "A certificate for paid-up shares in a corporation is simply a written statement in the name of the corporation that the holder thereof is a stockholder, and that the full par value of his shares has been paid to the corporation. If the shares in fact have not been so paid for, the certificate that they have been is a false representation that the assets of the corporation have been increased to the amount of the par value of the stock so issued. And, when a corporation represents that it has a paid-up capital of a given amount, it represents to the business world that at the time it issued the stock it received money or property to the full par value of its stock. The issuing of the stock of a corporation as paid-up when it is not so in fact is a public and a private wrong—a cheat and a fraud—which enables the corporation to obtain credit and property by false pretenses. Ethically, the legislature might with the same propriety authorize an individ-

It was held that the Illinois provision is intended to guard against the placing of worthless securities upon the market and not to interfere with the usual and customary methods of raising funds by railroad corporations for legitimate corporate purposes.[1] But stock issued in direct violation of a prohibitory statute is void,[2] and the holder has no standing in a court of equity.[3] It has been held that one who pays money for such stock under an agreement by which he has paid but fifty per cent. of the par value can not recover back the money he has actually paid, as he is *in pari delicto*.[4] But, somewhat inconsistently, it is held that a person who received bonus stock which was issued contrary to a prohibitory statute was liable to pay therefor in full.[5] If stock has once been fully paid and comes into the hands of the corporation, it may be reissued or distributed among the stockholders without violating the statute.[6] Good will is property for which stock in a corporation may be issued under the New York statute, which provides that no stock shall be issued for less than its par value and except for money, labor done or property actually received for the use and lawful purposes of the corporation.[7]

An agreement between the bondholders of an embarrassed railroad company provided that trustees should buy in the

ual to misrepresent his assets for the purpose of obtaining credit as to authorize a corporation, other than a mining corporation, to issue watered stock. Therefore, while the meaning of this statute is not entirely clear, it ought not to be construed, unless the express language used leaves us no other alternative, so as to impute to the legislature an intention to legalize a practice denounced by courts and text writers as immoral, contrary to public policy, and illegal, independent of any statute prohibiting it." Under this same statute it was held that an agreement between the subscribers that for each share paid for a certificate for two shares should be given was void. Rogers v. Gross, 67 Minn. 224.

[1] Peoria, etc., R. Co. v. Thompson, 103 Ill. 187. See Brown v. Duluth, etc., R. Co. (Minn.), 53 Fed. Rep. 889.

[2] Wood v Union, etc., Assn., 63 Wis. 9, 22 N. W. Rep. 756.

[3] Arkansas, etc., R. Co. v. Farmers', etc., Co., 13 Colo. 587.

[4] Clarke v. Lincoln, etc., Co., 59 Wis. 655, 18 N. W. Rep. 492. But see § 323, and cases cited.

[5] Richardson's Exs. v. Green, 133 U. S. 30.

[6] Commonwealth v. Boston, etc., R. Co., 142 Mass. 146; Davis Bros. v. Montgomery, etc., Co., 101 Ala. 127.

[7] Washburn v. National, etc., Co., 81 Fed. Rep. 17. See 33 Am. L. Rev. 581.

mortgaged property on foreclosure and convey it to a new company to be organized by the bondholders which should issue new mortgage bonds to pay the expenses of the sale, and other new mortgage bonds to be taken by the bondholders in lieu of their old bonds, and full paid-up stock subject to the mortgage debt, to be delivered to and held by the bondholders without any payment of money. It was held that the constitutional provision that "no private corporation shall issue stock or bonds except for money, on property actually received, or labor done, and all fictitious increase of stock or indebtedness shall be void" did not apply.[1] "It is not clear," said the court, "from the words used, that the framers of that instrument intended to restrict private corporations, at least when acting with the approval of their stockholders, in the exchange of their stock or bonds for money, property or labor, upon such terms as they deem proper; provided always, the transaction is a real one, based on a present consideration, and having reference to legitimate corporate purposes, and is not a mere device to evade the law and accomplish that which is forbidden. We can not suppose that the scheme whereby the appellant acquired the property, rights and privileges in question, for a given amount of its stock and bonds, falls within the prohibition of the state constitution. The beneficial owners of such interests had the right to fix the terms upon which they would surrender those interests to the corporation of which they were to be the sole stockholders."

[1] Memphis, etc., Railroad v. Dow, 120 U. S. 287.

CHAPTER 14.

STOCK SUBSCRIPTIONS.

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§ 343. **In general.**—A subscription to the capital stock of a corporation, already in being, is a contract between the corporation and the subscriber, and to be effectual, it must contain all the elements of an ordinary contract such as competent parties, mutuality and a consideration. But a subscription or agreement to subscribe to the stock of a corporation to be organized in the future is a mere offer to enter into a contract, and is not binding until the corporation is organized and the offer accepted. It is, therefore, necessary to distinguish between contracts of subscription for the stock of an existing corporation and an agreement to take stock in a corporation which it is contemplated shall be organized in the future.

§ 344. **Agreement to take shares in a corporation to be organized.**—Subscriptions are often made to the stock of a corporation which is in process of organization. When the statute provides for commissioners, who are authorized to take subscriptions under such circumstances and the provisions of the statute are complied with, the agreements are binding without reference to the question of consideration.[1] A preliminary agreement by a number of persons to form a corporation and to take stock therein, if made as a step authorized by a statute in the process of forming a corporation, is valid by virtue of the statute, although there is no consideration or mutuality prior to the organization of the corporation, and is binding and irrevocable from time of signing.[2] Such subscriptions are for the benefit of the corporation, and can only be enforced by it, although their validity is determined by the statute and not by the common law principles which govern a subscription to the stock of an existing corporation. Thus, where the subscription was made in the books of commissioners, authorized by statute, to take subscriptions, the court said: "The rules of common law in regard, consideration and mutuality do not apply to the case. These rules, I think, may be regarded as superseded by a statute which not only expressly authorizes subscriptions to

[1] Walter A. Wood, etc., Co. v. Robbins, 56 Minn. 48.

[2] Union, etc., Co. v. Jenkins, 1 Caines Cas. (N. Y.) 86; Taggart v. Western, etc., R. Co., 24 Md. 563.

be made in anticipation of the existence of a corporation, but impliedly at least recognizes their validity, but even without this clause it would, I think, be held that a statute which authorizes subscriptions in view of subsequent incorporation, and regulates the manner in which they shall be made, must necessarily have the effect to give validity to such subscriptions, if made in accordance with the requirements of the act.[1] It has been held that the agreement to associate together under the act to accomplish the purposes designed, would seem a sufficient consideration. The consideration need not move from the party with whom the contract is made. The consideration for one promise is that others will make like promises."[2]

A promise to take stock, before the articles of incorporation have been signed, does not constitute a subscription,[3] as such preliminary subscriptions are mere offers which must be accepted by the corporation before they become binding contracts.[4] "A subscription by a number of persons to the stock of a corporation to be thereafter formed by them has in law a double character. First, it is a contract between the subscribers themselves to become stockholders without further act on their part immediately upon the formation of the corporation. As such a contract it is binding and irrevocable from the date of the subscription (at least in the absence of fraud or mistake), unless canceled by consent of all the subscribers before acceptance by the corporation. Second, it is also in the nature of a continuing offer to the proposed corporation, which, upon acceptance by it after its formation, becomes as to each subscriber a contract between him and the corporation."[5] A mutual agreement to subscribe for stock in a corporation has been held to contemplate the further act

[1] Buffalo, etc., R. Co. v. Dudley, 14 N. Y. 336. See Sedalia, etc., R. Co. v. Wilkerson, 83 Mo. 235, Wilgus' Cases.

[2] Kennebec, etc., R. Co. v. Palmer, 34 Me. 366; Osborn v. Crosby, 63 N. H. 583; West v. Crawford, 80 Cal. 19; Twin Creek, etc., Co. v. Lancaster, 79 Ky. 552.

[3] Fanning v. Insurance, etc., Co., 37 Ohio St. 339; Thresher v. Pike Co. R. Co., 25 Ill. 340; California, etc., Co. v. Schafer, 57 Cal. 396.

[4] Starrett v. Rockland, etc., Co., 65 Me. 374.

[5] Minneapolis, etc., Co. v. Davis, 40 Minn. 110; Red Wing, etc., Co. v. Friedrich, 26 Minn. 112; Richelieu, etc., Co. v. International, etc., Co., 140 Ill. 248.

of executing a contract of subscription upon the stock books, and until this is done there is no offer which the corporation can accept.[1]

§ 345. **When there are no statutory provisions.**—An agreement by a number of persons to take stock in a corporation to be formed, when not a step authorized by statute in the organization of a corporation, is not a contract of the subscribers with each other, but is a mere continuing offer to the corporation by each subscriber, and may be revoked, or will lapse on the subscriber's death or insanity at any time before the corporation is organized. If the organization is perfected before the offer is revoked, it operates as an acceptance, and the subscription becomes irrevocable, the subscriber is a stockholder, and the subscription may be enforced by the corporation.[2] In jurisdictions where an action can be maintained by a third person upon a contract made for his benefit, the corporation after it is formed may maintain an action upon the contract.[3] In Massachusetts it was said: "In agreements of this nature entered into before the organization is formed or the agent constituted to receive the amount subscribed, the difficulty is to ascertain the promisee in whose name alone suit can be brought. The promise of each subscriber, to and with each other, is not a contract capable of being enforced, or intended to operate literally as a contract to be enforced between each subscriber and each other who may have signed previously, or who should sign afterwards; nor between each subscriber and all the others collectively as individuals. The undertaking is inchoate and incomplete as a contract until the contemplated organization is effected or the mutual agent is constituted to

[1] Athol, etc., Co. v. Carey, 116 Mass. 471; Lake Ontario, etc., R. Co. v. Curtiss, 80 N. Y. 219.

[2] Athol, etc., Co. v. Carey, 116 Mass. 471; Red Wing, etc., Co. v. Friedrich, 26 Wis. 112; Buffalo, etc., R. Co. v. Dudley, 14 N. Y. 336; Richilieu, etc., Co. v. International, etc., Co., 140 Ill. 248; Maysville, etc., Co. v. Johnson, 93 Cal. 538; Bullock v. Turnpike Co., 85 Ky. 184; McClure v. Railway Co., 90 Pa. St. 269; Shober's Admrs. v. Lancaster Co., etc., Assn., 68 Pa. St. 429.

[3] Marysville, etc., Co. v. Johnson, 93 Cal. 538; Int., etc., Assn. v. Walker, 83 Mich. 386, 47 N. W. Rep. 338.

represent the association of individual rights in accepting and acting upon the propositions offered by the several subscriptions. When thus accepted, the promise may be construed to have legal effect according to its purpose and intent, and the practical necessity of the case; to wit, as a contract with the common representative of the several associates.'"[1] It was held that an action might be maintained in the name of the corporation after it was organized against a subscriber upon the allotment to him of the shares subscribed for.

§ 345*a*. **Statement of rules.**—Professor Collin states the law on this subject as follows: "The following propositions are given as the substantially harmonious net result of much confusion in cases and text-books. Rambling remarks may be found contrary to each proposition, but very few reported cases have been decided contrary to any one of these propositions upon the facts coming within it, and I believe every proposition can be sustained in any state or federal court:

"(*a*) A preliminary agreement to form a corporation and take stock therein is not a contract by the subscribers with each other, and can not be enforced by one or more against any other, but only by the corporation.

"(*b*) Such an agreement not made as a step authorized by statute in the process of forming the corporation is a mere offer to the corporation not yet in existence, and is revocable by any subscriber until the birth of the corporation, which operates as an acceptance of the offer, and thereafter the subscription, if not previously revoked, is irrevocable, and may be enforced by the corporation.

"(*c*) Such an agreement made as a step authorized by statute in the process of forming the corporation is made valid by the statute, and is binding upon each subscriber from the time of signing, and is irrevocable thereafter, but can be enforced only by the corporation.

"(*d*) An agreement to pay money to trustees to be by them paid to a corporation thereafter to be created, the trustees to return to the subscribers stock in the corporation ac-

[1] Athol, etc., Co. v. Carey, 116 Mass. 471.

cordingly, is a valid contract between the subscribers and the trustees.

"(*e*) The distinction made between a present subscription and an agreement to subscribe to the stock of a corporation thereafter to be created is unsound in principle, and disappears as mere *dicta* upon a thorough sifting of the cases.[1]

"(*f*) The damages recoverable by the corporation upon a subscription is the amount of the subscription; and all discussion of any other measure of damages, such as the difference between the par and market value of stock subscribed, arises from a misconception of the situation and disappears from the net result of the authorities."[2]

§ 346. **Who may subscribe.**—Any one who is competent to enter into a common-law contract may make a valid subscription to the stock of a corporation. But the corporation can not be a subscriber to its own stock,[3] and by the weight of authority a corporation can not subscribe for the shares of another corporation without express authority. A subscriber may be a non-resident or an alien;[4] or it may be a municipal or public corporation when acting under proper statutory authority.[5] A state may debar aliens from holding shares of stock in a corporation, or it may admit them upon prescribed conditions.[6] A subscription may be made by a person under disability, but as in the case of other such contracts it may be repudiated within a reasonable time after the disability is removed. Whether a valid subscription may be made by a married woman will depend entirely on the extent to which her

[1] This distinction, however, is still recognized in the late case of Yonkers Gazette Co. v. Taylor, 30 App. Div. Rep. (N. Y.) 334 on 337 (1898).

[2] See Cook. Corp. (4th ed.), § 75.

[3] Talmage v. Pell, 7 N.Y. 328; Franklin Co. v. Lewiston Inst. for Sav., 68 Me. 43; Holladay v. Elliott, 8 Ore. 84; Allibone v. Hager, 46 Pa. St. 48.

[4] Commonwealth v. Hemingway, 131 Pa. St. 614, 18 Atl. Rep. 990.

[5] In Nassau Bank v. Jones, 95 N. Y. 115, it was said: "It is conclusively settled that municipal corporations may lawfully subscribe to the stock of private corporations, when authorized by statute to do so. It is not equally clear that one private corporation may subscribe for the stock in another corporation. On the contrary such subscriptions are *ultra vires* and void." Denny Hotel Co. v. Schram, 6 Wash. 134.

[6] State v. Travelers, etc., Co., 70 Conn. 590, 66 Am. St. Rep. 138.

common-law disabilities have been removed by statute. By the common law a subscription by a married woman is invalid.[1] The statute imposing individual responsibility to the amount of the par value of their shares upon all stockholders in national banks makes no exceptions in favor of married women;[2] and under a statute which provides that no woman, during coverture, shall be capable of making any contract to affect her real and personal estate without the written consent of her husband, it was held that a purchase of stock by a married woman is not a "contract" within the terms of the statute, and that the wife is liable for an assessment, although the stock was purchased without the consent of her husband. "If a purchase of stock in a national bank by a married woman without the written consent of her husband gives her the ownership of such stock, judgment must be given against the *feme* defendant. If she owned the stock at the failure of the bank, she is liable to the assessment; if she did not, she is not liable. While the federal government exclusively controls the question of the liability of stockholders in national banks, it is not doubted that a state has power to say that, for reasons seeming good to its legislature, and not in conflict with organic law, a particular class of persons shall not be permitted to own particular classes of property. * * * It certainly is nowhere enacted directly that a married woman shall not own stock in national banks, or stock that upon the failure of the corporation shall be liable to assessment."[3] The right to take stock in a certain kind of corporation may be restricted by express provision of the charter to persons of a certain nationality.[4]

§ 347. **Subscriptions through an agent.**—A valid contract of subscription may be made through a duly authorized agent.[5] In some states it is held that a person who assumes to act as

[1] Nat'l Com. Bank v. McDonnell, 92 Ala. 387.

[2] Keyser v. Hitz, 133 U. S. 138.

[3] Robinson v. Turrentine, 59 Fed. Rep. 554.

[4] Blien v. Rand (Minn., 1899), 79 N. W. Rep. 606.

[5] Barr v. Wilcox, 22 N. Y. 551; McClelland v. Whitely, 15 Fed. Rep. 332.

an agent for another without authority binds himself as a principal. Under such circumstances, the agent would become a stockholder in the corporation.[1] In other jurisdictions it is held that the agent does not become a stockholder, and is merely liable to the corporation in an action for damages.[2]

§ 348. **The form of the contract.**—A contract of subscription for shares in a corporation need not be in writing,[3] although, under particular charters, it has been held otherwise.[4] Irregularities are generally disregarded, and if it is clear that the party intended to bind himself the lack of form will not defeat his intention. Thus, a party was held bound by a subscription made in a memorandum book,[5] or upon a loose sheet of paper,[6] although the charter provided for opening subscription books.[7]

Generally, the fact that the form of subscription prescribed by the charter is not followed, will not invalidate the subscription,[8] although a form provided by the charter is of course sufficient.[9] The subscriber can not escape liability by showing that he has not performed conditions precedent which are prescribed by the charter, when it would result in injury to others who have in good faith acted upon his agreement.[10]

[1] State v. Smith, 48 Vt. 266; Nat'l Com. Bank v. McDonnell, 92 Ala. 387, 9 So. Rep. 149; Allibone v. Hagar, 64 Pa. St. 48.

[2] Salem Milldam Corp. v. Ropes, 9 Pick. (Mass.) 187. See Perkins v. Savage, 15 Wend. 412.

[3] York, etc., Assn. v. Barnes (Neb.), 58 N. W. Rep. 440; Colfax, etc., Co. v. Lyon, 69 Iowa 683, 29 N. W. Rep. 780; Des Moines Bank v. Colfax Hotel Co., 88 Iowa 4; Bullock v. Falmouth, etc., Co., 85 Ky. 184, 3 S. W. Rep. 129; National Bank v. Van Drewerker, 74 N. Y. 234. See § 286.

[4] Fanning v. Insurance Co., 37 Ohio St. 339; Galveston Hotel v. Bolton, 46 Tex. 633; Vreeland v. New Jersey, etc., Co., 29 N. J. Eq. 188.

[5] Buffalo, etc., Co. v. Gifford, 87 N. Y. 294.

[6] Iowa, etc., R. Co. v. Perkins, 28 Iowa 281.

[7] Ashtabula, etc., R. Co. v. Smith, 15 Ohio St. 328.

[8] Rensselaer, etc., Co. v. Barbon, 16 N. Y. 457, note; Home, etc., Co. v. Sherwood, 72 Mo. 461; Webb v. Baltimore, etc., R. Co., 77 Md. 92; Pittsburgh, etc., R. Co. v. Applegate, 21 W. Va. 172; Illinois, etc., R. Co. v. Zimmer, 20 Ill. 654.

[9] Parker v. Northern, etc., R. Co., 33 Mich. 23.

[10] Wood v. Coosa, etc., R. Co., 32 Ga. 273; Boyd v. Peach Bottom R. Co., 90 Pa. St. 169. If the name of a person appears on the stock book

§ 349. **The consideration.**—A subscription for shares confers mutual rights. The advantages arising from membership in the corporation, and interest in the property and franchises and the right to participate in dividends is a sufficient consideration to support the contract.[1] "The subscription for the stock constitutes a contract with the company which is supported by a sufficient consideration. The subscriber thereby acquires an interest in the corporation and there is an implied promise on the part of the company to issue the proper certificates, as evidence of his interest, whenever the terms of his subscription shall be complied with, so as to entitle him to it."[2] When the subscription contract is made with the corporation or its agents,[3] or is subsequently accepted by the corporation[4] the implied counter promise of the corporation is a sufficient consideration to uphold the contract.[5] The legislature may make subscriptions preliminary to the organization of the corporation binding without reference to the consideration.[6] Such subscriptions are binding by virtue of the statute. When subscriptions were made in the books of commissioners who were provided for by the statute, it was said that the subscriptions could not be revoked, even before the corporation was organized. The court said: "The rules of the common law in regard to consideration and mutuality do not apply to the case. These rules may, I think, be regarded as superseded by the statute, which not only expressly authorizes subscriptions to

of a corporation as a stockholder, though the book is irregularly kept and does not contain the entries prescribed by statute, the presumption is that he is the owner of the stock, and the burden is on him to show that he is not a stockholder. Holland v. Duluth, etc., Co., 65 Minn. 324.

[1] Mahan v. Wood, 44 Cal. 462; Cottage St., etc., Church v. Kendall, 121 Mass. 528; Athol, etc., Co. v. Carey, 116 Mass. 471.

[2] Walter A. Wood, etc., Co. v. Robbins, 56 Minn. 48, 57 N. W. Rep. 317.

[3] Lake Ontario, etc., R. Co. v. Curtiss, 80 N. Y. 219; Wallace v. Townsend, 43 Ohio St. 537; Parker v. N. Cent. R. Co. 33 Mich. 23.

[4] N. Cent. R. Co. v. Eslow, 40 Mich. 222.

[5] Kennebec, etc., R. Co. v. Jarvis, 34 Maine 360. See Starratt v. Rockland, etc., Co., 65 Maine 374; University of Des Moines v. Livingston, 57 Iowa 307.

[6] See § 344.

be made in anticipation of the existence of the corporation, but impliedly, at least, recognizes their validity."[1]

§ 350. **Signing articles of incorporation.**—A valid subscription may be made by signing the articles of association and writing after the signature the number of shares taken. Such an agreement does not become enforcible until the articles are acknowledged as required by statute.[2] The rule stated in the preceding section applies also to subscriptions made by signing the articles of incorporation, or a formal subscription paper which is required to be filed by the statute. It can not be revoked, as the subscription is presumed to be accepted by the corporation and takes effect from the filing of the certificate required by statute.

§ 351. **Application, allotment and notice.** — Where the method of taking stock is by application, allotment and notice, the notice is of the essence of the contract, and the contract dates from the mailing of the notice and is complete whether it reaches the allottee or not.[3]

§ 352. **Conditional subscriptions.**—A conditional subscription is one on which payment can be enforced by the corporation only after the occurrence or after the performance by the corporation of certain things specified in the subscription itself.[4] Such a subscription is merely an offer to become a member of the corporation after the condition is performed, and until the condition is performed the subscriber does not become a stockholder in the corporation.[5] Thus, a subscription for

[1] Buffalo, etc., R. Co. v. Dudley, 14 N. Y. 336.

[2] Coppage v. Hutton, 124 Ind. 401, 7 L. R. A. 591; Cravens v. Cotton Mills, 120 Ind. 6; Nulton v. Clayton, 54 Iowa 425; Phœnix, etc., Co. v. Badger, 67 N. Y. 294; Dayton v. Borst, 31 N. Y. 435; Joy v. Manion, 28 Mo. App. 55; Lake Ontario, etc., R. Co. v. Mason, 16 N. Y. 451; Greenbrier Ind. Expo. v. Rodes, 37 W. Va. 738.

[3] Pellatt's Case, 2 Ch. App. Cas. 527; In re Northern, etc., Co., Ch. Div. 8 R. Corp. L. J. 177. This method is peculiar to English law.

[4] Montpelier, etc., R. Co. v. Langdon, 46 Vt. 284.

[5] Ticonic, etc., Co. v. Lang, 63 Me. 480. There can not be such a thing as a "conditional membership." Pittsburgh, etc., R. Co. v. Biggar, 34 Pa. St. 455.

shares in a railway corporation, upon condition that the road shall be located upon a certain route, is a conditional subscription, and the subscriber does not become a member until the road has been so located.[1] In New York such a condition to a subscription made before incorporation renders the subscription void,[2] while in Pennsylvania it is held that "where one subscribes to the stock of a private corporation prior to the procurement of its charter, such subscription is to be regarded as absolute and unqualified, and any condition attached thereto is void."[3] Of conditional subscriptions before incorporation, the supreme court of the United States said that where "the law prescribes that a certain amount of stock shall be subscribed before corporate powers shall be exercised, if subscriptions, obtained before the organization was effected, may be subsequently rendered unavailable by conditions attached to them, the substantial requirements of the law are defeated. The purpose of such a requirement is that the state may be assured

[1] Swartwout v. Mich., etc., R. Co., 24 Mich. 389; Taggart v. Western, etc., R. Co., 24 Md. 563. In McMillan v. Maysville, etc., R. Co., 15 B. Mon. (Ky.) 218, the court said: "When the road was * * * located, signers became unconditional stockholders, and as such were entitled to all the corporate rights and privileges of members of the company. The stock itself was not conditional; it was only the agreement to take it that was conditional. The subscribers were not stockholders until the company had performed the condition upon which their undertaking depended; and when that was done they became stockholders by force of the agreement of the parties." In Vent v. Duluth, etc., Co., 64 Minn. 307, it was held that an agreement for the purchase from the corporation of its shares, with a provision that the purchaser may return the stock and receive his money back within a certain time, is a conditional sale and enforcible between the parties.

[2] Butternuts, etc., Co. v. North, 1 Hill (N. Y.) 518; Troy, etc., R. Co. v. Tibbits, 18 Barb. 297; In re Rochester, etc., R. Co., 50 Hun 29; Ft. Edwards, etc., Road Co. v. Payne, 15 N. Y. 583. See Putnam v. City of New Albany, 4 Biss. 365.

[3] Caley v. Philadelphia, etc., R. Co., 80 Pa. St. 363; Boyd v. Peach Bottom R. Co., 90 Pa. St. 169; Burke v. Smith, 16 Wall. 390; Pittsburgh, etc., R. Co. v. Bigger, 34 Pa. St. 455. A conditional subscription before incorporation may be treated as a continuing offer to take shares upon the terms indicated, and if not withdrawn may be accepted by the proper agent of the corporation after its organization. A subscription upon special terms, received after organization by an agent without authority, may, if not withdrawn, be accepted by the board of directors. Red Wing, etc., Co. v. Friedrich, 26 Minn. 112.

of the successful prosecution of the work, and that creditors of the company may have, to the extent, at least, of the required subscription, the means of obtaining satisfaction of their claims. The grant of the franchise is, therefore, made dependent upon securing a specified amount of capital. If the subscriptions to the stock can be clogged with such conditions as to render it impossible to collect the fund which the state requires to be provided before it would assent to the grant of corporate powers, a charter might be obtained without any available capital. Conditions attached to subscriptions, which, if valid, lessen the capital of the company, thus depriving the state of the security it exacted that the railroad would be built, and diminishing the means intended for the protection of creditors, are, therefore, a fraud upon the grantor of the franchise and upon those who may become creditors of the corporation. They are also a fraud upon unconditional stockholders, who subscribed for the stock in the faith that capital would be obtained to complete the projected work, and who may be compelled to pay their subscriptions, though the enterprise has failed, and their whole investment has been lost. It is for these reasons that such conditions are denied any effect."[1] But, after incorporation, conditional subscriptions are held valid in all the states,[2] and a conditional subscription, which the corporation has no authority to accept at the time, will constitute a continuing offer, and, if not withdrawn before the conditions are performed, it will become absolute and binding.[3] A stipulation in a contract of subscription that the subscriber shall receive bonds of the corporation as a bonus in an amount equal to the stock for which he subscribes does not make the issuance of the bonds a con-

[1] Burke v. Smith, 16 Wall. 390.

[2] Pittsburgh, etc., R. Co. v. Stewart, 41 Pa. St. 54; Hanover, etc., R. Co. v. Haldeman, 82 Pa. St. 36; Baltimore, etc., R. Co. v. Pumphrey (Md.), 21 Atl. Rep. 559; Armstrong v. Karshner, 47 Ohio St. 276, 24 N. E. Rep. 897; Carey & Co. v. Morrill, 61 Vt. 598; Taggart v. Railroad Co., 24 Md. 563; Webb v. Railway Co., 77 Md. 92. In New York, however, it is held that the condition that a railroad shall be located over a particular route is invalid as against public policy. Butternuts, etc., R. Co. v. North, 1 Hill 518.

[3] Armstrong v. Karshner, 47 Ohio St. 276, 24 N. E. Rep. 897.

dition precedent to liability on the subscription contract. The liability exists, although the corporation fails to carry out the agreement. Such an agreement is void.[1]

§ 353. **Secret conditions.**—Conditions attached to subscriptions must be included in the written agreement, as oral conditions can not be shown.[2] A secret agreement between the subscriber and the corporation which in effect changes the ostensible terms of the subscription is void. The corporation may disregard the collateral agreement and hold the subscriber to the ostensible contract.[3] The only exception to this rule seems to be found in Pennsylvania, where it may be shown by oral evidence that a written subscription, absolute on its face, was in fact conditional. But an agreement to which the corporation and all the subscribers for stock are parties that a subscriber shall not be required to pay for his shares is binding when there are no creditors. There is no liability as between such a subscriber and the other shareholders.[4] A party can not defend on the ground that his subscription was feigned and fraudulent, and that the corporation was a party to the fraud.[5]

[1] Morrow v. Nashville, etc., Co., 87 Tenn. 262, 3 L. R. A. 37.

[2] Minneapolis, etc., Co. v. Davis, 40 Minn. 110; Masonic Temple Assn. v. Channell, 43 Minn. 353; Hoskell v. Sells, 14 Mo. App. 91; Nippenose, etc., Co. v. Stadon, 68 Pa. St. 256; Miller v. Hanover Junction, etc., R. Co., 87 Pa. St. 95; Baile v. Educational Society, 47 Md. 117; Galena, etc., R. Co. v. Ennor, 116 Ill. 55; Downie v. White, 12 Wis. 176; Topeka, etc., Co. v. Hale, 39 Kan. 23. As to parol declarations by officers of the corporation which amount to fraud, see Martin v. Pensacola, etc., R. Co., 8 Fla. 370. By promoters as to the proposed route of a railroad, Braddock v. Philadelphia, etc., R. Co., 45 N. J. L. 363.

[3] Meyer v. Blair, 109 N. Y. 600; White Mountain R. Co. v. Eastman, 34 N. H. 124; Jewell v. Rock River P. Co., 101 Ill. 57; Melvin v. Lamar, etc., Co., 80 Ill. 446; Winston v. Dorsett, etc., Co., 129 Ill. 64; Piscataqua, etc., Co. v. Jones, 39 N. H. 491.

[4] Winston v. Rock River P. Co., 129 Ill. 64, 4 L. R. A. 507.

[5] Graff v. Pittsburg, etc., R. Co., 31 Pa. St. 489; Phœnix W. Co. v. Badger, 67 N. Y. 294. A subscription on a blank piece of paper on condition that it will not be attached to the articles of incorporation until they are presented to the subscriber for his approval is held valid in Bucher v. Dillsburg, etc., R. Co., 76 Pa. St. 306, and see Great, etc., Co. v. Loewenthal, 154 Ill. 261.

§ 354. **Subscription of amount named in charter or required by law.**—When a subscription is made upon condition that a certain amount of stock shall be subscribed, the subscriber can not be called on until the full amount is taken.[1] If the amount of capital stock of a corporation is named in its charter, it by implication has no authority to begin business until the whole amount of such capital has been subscribed, and the stockholders can not be required to pay their subscriptions until the full amount of capital is legally subscribed[2] by solvent persons apparently able to pay for the shares.[3] "It is an implied part of the contract of subscription that the contract is to be binding and enforcible against the subscriber only after the full capital stock of the corporation has been subscribed. This condition precedent to the liability of the subscriber need not be expressed in the corporate charter or the subscription itself. It arises by implication from the just and reasonable understanding of a subscriber that he is to be aided by other subscriptions. This rule is supported by public policy, in that corporate creditors have a right to rely upon a belief that the full capital stock of a corporation has been subscribed."[4]

[1] Philadelphia, etc., R. Co. v. Hickman, 28 Pa. St. 318; Union, etc., Co. v. Hersee, 79 N. Y. 454. As to necessary allegation in the complaint, see Duluth, etc., Co. v. Witt, 63 Minn. 538.

[2] Anderson v. Railroad Co., 91 Tenn. 44, 17 S. W. Rep. 803; Anvil, etc., Co. v. Sherman, 74 Wis. 226, 42 N. W. Rep. 226; Masonic, etc., Assn. v. Channell, 43 Minn. 353; Boston, etc., R. Co. v. Wellington, 113 Mass. 79; Denny, etc., Co. v. Schram, 6 Wash. 134, 36 Am. St. Rep. 130; Salem, etc., Corp. v. Ropes, 6 Pick. 23, 19 Am. Dec. 363; Livesey v. Omaha Hotel, 5 Neb. 50; Peoria, etc., R. Co. v. Preston, 35 Iowa 118; Atlantic, etc., Mills v. Abbott, 9 Cush. (Mass.) 423; International Fair, etc., Assn. v. Walker, 88 Mich. 62; Katama, etc., Co. v. Jernegan, 126 Mass. 155; Johnson v. Shar, 9 S. Dak. 536; Hendrix v. Academy of Music, 73 Ga. 437; Allman v. Havana, etc., R. Co., 88 Ill. 521. *Contra*, Nelson v. Blakey, 54 Ind. 29.

[3] Lewey's, etc., R. Co. v. Bolton, 48 Maine 451.

[4] Cook I, § 176; Stoops v. Greensburgh, etc., Co., 10 Ind. 47. The right to levy a preliminary assessment to defray the expenses of incorporation does not imply the right to levy subsequent assessments before the full required amount of capital is subscribed. In Anvil, etc., Co. v. Sherman, 74 Wis. 226, 4 L. R. A., 232, the court said: "The first position, that before the cor-

Such an implication is overcome if the terms of the subscription contract or of the statute under which the corporation is organized is inconsistent with the existence of such a condition.[1] But the rule that "when the capital stock is fixed by the charter, an action does not lie to enforce a subscription until all the stock is taken, does not apply where, from the face of the charter, it is obvious that the whole of the capital stock was not necessary to the organization of the company, and the subscriber knew, or had reason to know, this at the time of subscribing; nor does it apply where a subscriber takes part in carrying on the business of the company, and votes on his shares; at least, when the suit is brought by the receiver of the corporation after it has become insolvent."[2]

The condition may of course be waived by the subscriber.[3] The amount which has been subscribed may be shown by the

poration can make an assessment after the first for preliminary objects has been made, the whole of the capital stock must have been taken or subscribed, is unquestionably sustained by nearly all the authorities in this country. * * * There is a principle recognized in these decisions that, outside the language of the subscription itself, the provisions of the charter and of the statute are to be considered in construing and giving effect to the contract of subscription. From the whole, taken together, this condition of full subscription and the limitations upon the liability of stockholders are derived. It is by no means an end of the question that the subscription itself is absolute and unconditional; and yet some cases cited by the learned counsel for the respondent are rested entirely upon the language of the contract of subscription, and because no condition is found therein, they hold that there is none. The distinction in all the cases is that the first call or assessment which is supposed to be paid at once, or within a very short time, is unconditional, and must be paid in order to meet the preliminary and incidental expenses of organizing the corporation, and getting it into a condition to transact its general business and carry out its general objects. The leading authority upon this question, and which has been followed by nearly all the subsequent cases in this country, is the case of Salem, etc., Corp. v Ropes, 6 Pick. 23, 19 Am. Dec. 363."

[1] Lincoln, etc., Co. v. Sheldon, 44 Neb. 279; Anderson v. Railroad Co., 91 Tenn. 41; Iowa, etc., R. Co. v. Perkins, 28 Iowa 281; Arkadelphia, etc., Mills v. Trimble, 54 Ark. 316; Port Edward R., etc., Co. v. Arpin, 80 Wis. 214, 49 N. W. Rep. 828.

[2] Taylor Priv. Corp., § 518; Musgrave v. Morrison, 54 Md. 161.

[3] Masonic, etc., Assn. v. Channell, 43 Minn. 353; Cornell & Michler's Appeal, 114 Pa. St. 153; Hamilton v. Railroad Co., 144 Pa. St. 34; Anderson v. Railroad Co., 91 Tenn. 44; Gibbons v. Ellis, 83 Wis. 434.

records of the corporation.[1] But the certificate of commissioners appointed by the legislature to take subscriptions that the required amount has been subscribed is conclusive.[2]

§ 355. **Payment of deposit.**—It is not uncommon for the statute or corporate charter to provide that a certain percentage of the amount of the subscription shall be paid at the time the subscription is made. It is held by one line of decisions that when the subscription is prior to incorporation a failure to comply with this requirement renders the subscription void.[3] Another line of decisions holds that the provision is for the benefit of the corporation, and that it may therefore be waived by it, and that, as the subscriber will not be permitted to take advantage of his own neglect, the contract is enforcible.[4] When the subscription is made after the corporation is organized, the requirement, being for the benefit of the corporation alone, may be waived by it unless the contrary appears to have been clearly the legislative intention.[5] Unless the law expressly requires payment to be made in cash, it may be made in services or in any other equivalent of cash.[6] Thus, payment may be made in a promissory note, accepted in good faith, but not in a check, although indorsed, which it is agreed shall not be presented for payment.[7]

§ 356. **Tender of certificate.**—It is not necessary that a certificate of stock should have been issued in order to make a subscriber a member of the corporation and liable on his subscription.[8] "A certificate of the shares of stock in a corpora-

[1] Penobscot R. Co. v. Dummer, 40 Maine 172.

[2] Connecticut, etc., R. Co. v. Bailey, 24 Vt. 465.

[3] President, etc., Hibernia Road v. Hinderson, 8 Sargt. & Rawle (Pa.) 219; Beach v. Smith, 30 N. Y. 116; Taggart v. Railway Co., 24 Md. 563; New York, etc., Co. v. Van Horn, 57 N. Y. 473.

[4] Wight v. Railway Co., 16 B. Mon. (Ky.) 4; M. & St. L. R. Co. v. Bassett, 20 Minn. 536; Illinois, etc., R. Co. v. Zimmer, 20 Ill. 654.

[5] Taggart v. Railway Co., 24 Md. 563; Oler v. Railway Co., 41 Md. 593; Webb v. Railway Co., 77 Md. 92.

[6] Boyd v. Railway Co., 90 Pa. St. 169; Rothschild v. Hoge, 43 Fed. Rep. 97; Beach v. Smith, 30 N. Y. 116.

[7] Crocker v. Crane, 21 Wend. (N. Y.) 211.

[8] Holland v. Duluth, etc., Co., 68 N. W. Rep. 50; Chaffin v. Cummings, 37

tion is merely a solemn affirmation under the seal of the company that a certain amount of shares of stock stands in the name of the individual named in the certificate."[1] The execution of notes to the corporation in payment of an installment due on a subscription under a contract by which the shares are to be issued and held by the bank as security for the payment of the notes makes the subscriber a stockholder, although the certificate is not issued.[2] It is no defense to an action on the subscription that a certificate of stock has not been tendered to the subscriber.[3] Such a subscription is not a contract for the purchase of certificates, and the certificate is not necessary to make the subscriber a stockholder. "When a subscriber pays he is the owner of the stock; it is the payment that makes him a stockholder, the certificate being merely evidence of his right; that he is a full stockholder, with all the rights of one, even if a certificate is never issued to him; and, therefore, it is for him to demand a certificate when he wishes one, and not for the corporation to tender it."[4] The tender of a certificate may be made a condition by the terms of the contract.[5]

§ 357. **Conditional delivery of subscription contract.**—A written subscription may be delivered to a third person to take effect only on the performance of some condition. But if the delivery is to the corporation or its agent the contract is bind-

Maine 76; Haynes v. Brown, 36 N. H. 545; Butler University v. Scoonover, 114 Ind. 381; Mitchell v. Beckman, 64 Cal. 117; Pacific Nat'l Bank v. Eaton, 141 U. S. 227; Tennessee, etc., Co. v. Ayers (Tenn.), 43 S. W. Rep. 744.

[1] Shropshire, etc., R. Co. v. Queen, L. R. 7 H. L. 496.

[2] Glenn v. Rosborough, 48 S. C. 272.

[3] Chester, etc., Co. v. Dewey, 16 Mass. 94; Wemple v. Railroad Co., 120 Ill. 196; Rutter v. Kilpatrick, 63 N. Y. 604; Webb v. Railroad Co., 77 Md. 92; Courtright v. Deeds, 37 Iowa 503; Mitchell v. Beckman, 64 Cal. 117. But the corporation must be in a position to issue the certificate before it can recover on the subscription. Railway Co. v. Knoxville, 98 Tenn. 1.

[4] Marson v. Deither, 49 Minn. 423; Columbia, etc., Co. v. Dixon, 46 Minn. 463; Walter A. Woods Co. v. Robbins, 56 Minn. 48, 57 N. W. Rep. 317. These cases overrule St. Paul, etc., R. Co. v. Robbins, 23 Minn. 439, and Minneapolis, etc., Co. v. Libby, 24 Minn. 327, where the court adopted the view that the contract was for the purchase of the certificates of stock as securities. See Upton v. Tribilcock, 91 U. S. 45; Fulgam v. Macon, etc., R. Co., 44 Ga. 597.

[5] Marson v. Deither, 49 Minn. 423; Courtright v. Deeds, 37 Iowa 503.

ing from the time of such delivery.[1] In a case where the subscriber sought to escape liability by asserting that there had been no delivery of the subscription to the corporation, the court said that the promoter who "solicited and obtained the subscriptions occupied the position of agent for the subscribers as a body, to hold the subscriptions until the corporation was formed in accordance with the terms and conditions expressed in the agreement, and then turn it over to the company without any further act of delivery on the part of the subscribers. The corporation would then become the party to enforce the rights of the whole body of subscribers. It follows then that considering the subscriptions as a contract between the subscribers, a delivery to [the promoter] by a subscriber was a complete and valid delivery, so that his subscription became *eo instanti* a binding contract. The case stands precisely as a case where a contract is delivered by the obligor to the obligee."[2]

§ 358. **Performance of condition—Waiver.**—A conditional subscription must be accepted by the corporation, and the condition must be performed within a reasonable time.[3] The corporation has the burden of showing that the conditions have been performed,[4] or that performance thereof has been waived by the subscriber.[5] A waiver may be implied from the conduct of the subscriber, as by acting as a stockholder with full knowledge of all the facts, or part payment, but it can not be presumed from mere silence.[6] The subscriber may be estopped

[1] Wight v. Railroad Co., 16 B. Mon. (Ky.) 4.

[2] Minneapolis, etc., Co. v. Davis, 40 Minn. 110; Thresher v. Pike Co. R. Co., 25 Ill. 340; Quick v. Lemon, 105 Ill. 578. But see Cass v. Pittsburg, etc., R. Co., 80 Pa. St. 31, Wilgus' Cases.

[3] Johnson v. Kessler, 76 Iowa 411; Blake v. Brown, 80 Iowa 277, 45 N.W. Rep. 751; Stevens v. Corbitt, 33 Mich. 458; Lee v. Imbrie, 13 Ore. 510; California, etc., Co. v. Callender, 94 Cal. 120.

[4] Santa Cruz R. Co. v. Schwartz, 53 Cal. 106; People v. Holden, 82 Ill. 93.

[5] O'Donald v. Railroad Co., 14 Ind. 259; Hanover, etc., R. Co. v. Haldeman, 82 Pa. St. 36; Slipher v. Earhart, 83 Ind. 173; Parks v. Evansville, etc.. R. Co., 23 Ind. 567; Thomp. Corp., § 1336.

[6] Buckport, etc., R. Co. v. Brewer, 67 Maine 295; Cornell & Michler's Appeal, 114 Pa. St. 153, 6 Atl. Rep. 258; Mack's Appeal (Pa.), 7 Atl. Rep. 481.

by his actions from asserting that conditions have not been performed. Thus, one who subscribes for shares and joins in a certificate which sets forth the fact that all conditions precedent have been performed will not be heard to say that they have not been performed when sued on his contract of subscription.[1] So a shareholder who has participated in the business of the corporation can not assert that the entire capital was not subscribed.[2] A substantial compliance with the condition is sufficient.[3]

§ 359. **Conditions subsequent.**—A subscription may be made with an independent condition, for the non-performance of which the company is liable in damages, although the subscription itself is absolute and unconditional and enforcible regardless of the performance of the condition.[4] Whether a condition be "precedent or subsequent is a question purely of intention, and the intention must be determined by considering not only the words of the particular clause, but also the language of the whole contract, as well as the nature of the act required, and the subject-matter to which it relates."[5] Thus, where the subscription was to the stock of a hotel company upon condition that a hotel be built upon a designated lot or block, it was held that the building of a hotel was not a condition precedent to the right of the company to collect an assessment upon the stock, as it was obvious that it was the intention of the parties that the hotel should be built by the company out of the proceeds of the stock subscription.[6] As said in another case, where a similar defense was interposed, "it presupposes that the company was to build their road without money,

[1] Bavington v. Pittsburg, etc., R. Co., 34 Pa. St. 358.

[2] Stillman v. Dougherty, 44 Md. 380.

[3] Taggart v. Western Md. R. Co., 24 Md. 563; Junction R. Co. v. Reeve, 15 Ind. 236; Des Moines, etc. R. Co. v. Graff, 27 Iowa 99; Davenport, etc., R. Co. v. O'Connor, 40 Iowa 477; Missouri Pac. R. Co. v. Tygard, 84 Mo. 263.

[4] Belfast, etc., Co. v. Moore, 60 Maine 561; Milldam Foundry v. Hovey, 38 Mass. 417. As to what are such conditions, see Kansas City, etc., R. Co. v. Alderman, 47 Mo. 349; Kelsey v Northern, etc., Co., 45 N. Y. 505.

[5] Buckport, etc., R. Co. v. Brewer, 67 Maine 295; Lane v. Brainerd, 36 Conn. 565.

[6] Red Wing, etc., Co. v. Friedrich, 26 Minn. 112.

and to deliver it, a finished work, to the subscribers, who were then to pay their subscriptions."[1] The courts favor conditions subsequent.[2] Only the managing agents of a corporation have authority to accept subscriptions upon conditions precedent. Such contracts can not be made by commissioners prior to incorporation. But, in general, "subscriptions to the capital stock of a corporation may be conditioned as to the time, manner, or means of payment, or in any other way not prohibited by statute or the rules of public policy, and not beyond the corporate powers of the corporation to comply with."[3] If the condition is *ultra vires* or operates as a fraud upon the other stockholders or the creditors of the corporation, it is unenforcible, and the contract of subscription is enforcible without reference to the conditions.[4]

§ 360. **Subscriptions upon special terms.**—Subscriptions upon conditions subsequent are sometimes called subscriptions upon special terms. The subscription in such cases is absolute and the subscriber becomes a member of the corporation as soon as his subscription is accepted. An illustration of a subscription upon special terms is found where there is a subscription for shares in a railway company upon condition that payment may be made in railway ties. As said in one case: "A subscription on a condition subsequent contains a contract between the corporation and the subscriber whereby the corporation agrees to do some act, thereby combining two contracts, one, the contract of subscription, the other, an ordinary contract of a corporation to perform certain specified acts. The subscription is valid and enforcible whether the conditions are performed or not. The condition subsequent is the same as a separate collateral con-

[1] Miller v. Pittsburg, etc., R. Co., 40 Pa. St. 237.

[2] Swartwout v. Michigan, etc., Co., 24 Mich, 389.

[3] Cook Corps., § 83.

[4] Melvin v. Insurance Co., 80 Ill. 446; Meyer v. Blair, 109 N. Y. 600; York Park, etc., Assn. v. Barnes, 39 Neb. 834, 58 N.W. Rep, 440; Upton v. Tribilcock, 91 U. S. 45; Winston v. Dorsett, etc., Co., 129 Ill. 64, 21 N. E. Rep. 514.

tract between the corporation and the subscriber, for breach of which an action for damages is the remedy."[1]

If there is any doubt as to whether a condition was intended to be a condition precedent or subsequent it will be held to be a condition subsequent, that is a subscription upon special terms.[2] A contract of subscription provided that one fourth of the amount should be paid when the road was completed to the county line, and the balance "to be paid in four equal installments of four months as the work progresses through the county, provided the company establishes a depot on said road," at a designated point. The completion of the road to the county line was held to be a condition precedent to liability, but the provision for the construction of a depot was a collateral contract, the non-performance of which did not affect the subscriber's liability.[3]

§ 361. **Subscriptions in excess of authorized capital.**—Such subscriptions are void and no liability thereon attaches to the subscriber.[4] Before a subscriber can be required to pay there must be a distribution of the shares among those who are entitled to them.[5] In making the distribution the commissioners act judicially.[6] But it is no defense to an action against a subscriber for shares within the limit, that the corporation has issued stock in excess of the limit allowed by law.[7] Where the commissioners have power to apportion stock no subscription will be void, as each subscriber will then receive (unless the commissioners in the exercise of a lawful discretionary authority otherwise determine) such a proportion of the whole capital stock as his subscription bears to the whole amount subscribed.[8] But the commissioners must have statutory authority to make such apportionment.[9]

[1] Morrow v. Steel Co., 87 Tenn. 262.

[2] Paducah, etc., R. Co. v. Parks, 86 Tenn. 551, 8 S. W. Rep. 842.

[3] Paducah, etc., R. Co. v. Parks, 86 Tenn. 554.

[4] Lathrop v. Kneeland, 46 Barb. 432; Burrows v. Smith, 10 N. Y. 550; Clark v. Turner, 73 Ga. 1.

[5] Burrows v. Smith, 10 N. Y. 550; Buffalo, etc., Co. v. Dudley, 14 N. Y. 336.

[6] Crocker v. Crane, 21 Wend. 211.

[7] Oler v. Baltimore, etc., R. Co., 41 Md. 583.

[8] Buffalo, etc., Co. v. Dudley, 14 N. Y. 336.

[9] Van Dyke v. Stout, 8 N. J. Eq. 333; Lowell, § 116.

§ 362. **Amount of subscription by one person.**—Commissioners to take subscriptions may, without statutory authority, limit the number of shares that one person may take.[1] Although at common law one person might subscribe for the entire capital stock.[2]

§ 363. **Who may receive subscriptions.**—A subscription to be valid and binding upon the corporation must be taken by an authorized agent of the corporation or be subsequently ratified by it.[3] The statute sometimes provides that subscriptions shall be received through commissioners, but such provisions are directory only and subscriptions taken in other ways are valid.[4] The authority of such agents is determined by the statute. Acts in excess of the authority conferred by the statute are of no effect unless adopted by the corporation if within its power. A promoter of a proposed corporation who solicits and procures stock subscriptions is the agent of the body of the subscribers to hold the subscriptions until the corporation is formed, and then turn them over to it without further act of delivery on the part of subscribers.[5]

§ 364. **Subscriptions necessary to obtain charter.**—Where the law requires that a certain amount of capital stock shall be subscribed before a charter is granted, subscriptions which are merely colorable, or by persons having no reasonable expectation of being able to pay,[6] or without capacity to contract,[7]

[1] Brower v. Passenger R. Co., 3 Phil. 161; Perkins v. Savage, 15 Wend. (N. Y.) 412.

[2] King v. Barnes, 109 N. Y. 267.

[3] Walker v. Mobile, etc., R. Co., 34 Miss. 245; Taggart v. Western, etc., R. Co., 24 Md. 563.

[4] Buffalo, etc., R. Co. v. Gifford, 87 N. Y. 294; Croker v. Crane, 21 Wend. 211; Stuart v. Valley R. Co., 32 Gratt. 146. *Contra*, Schurtz v. Schoolcraft, etc., R. Co., 9 Mich. 269; Unity, etc., Co. v. Cram, 43 N. H. 636. As to powers of such commissioners, see Beach on Railways, § 84; Penobscot, etc., R. Co. v. White, 41 Me. 512; Croker v. Crane, 21 Wend. 211.

[5] Minneapolis, etc., Co. v. Davis, 40 Minn. 110.

[6] Holman v. State, 105 Ind. 569; Leweys Island R. Co. v. Bolton, 48 Maine 451; Penobscot R. Co. v. White, 41 Maine 512.

[7] Phillips v. Bridge Co., 2 Metc. (Ky.) 219; Appeal of Hahn (Pa.), 7 Atl. Rep. 482.

or upon special terms,[1] or *ultra vires*,[2] or conditional, can not be counted.[3] They must be binding subscriptions or they can not be included in the amount necessary to enable the corporation to collect its subscriptions and commence business. Subscriptions by an agent without authority may be counted in those jurisdictions in which the agent in such case binds himself, if not his principal.[4] Before conditional subscriptions can be taken into account the person seeking to enforce the subscription must make it appear that the conditions have been performed, and the subscription thus become absolute.[5]

§ 365. **Withdrawal of subscriptions—Notice.**—A subscription being, by the weight of authority, a mere offer, may be withdrawn at any time before incorporation, notwithstanding the fact that the subscriber has been active in inducing others to subscribe, and that his associates have incurred obligations upon the strength of his subscription.[6] A subscription lapses by the death of the subscriber before the corporation is organized and accepts the offer.[7] The right to withdraw ceases when the offer is accepted. It can thereafter be withdrawn only with the consent of the corporation and all the other subscribers.[8] Notice of the withdrawal is usually given to the same person to whom the application for shares was made. Where the articles of incorpora-

[1] Boston, etc., R. Co. v. Wellington, 113 Mass. 79; Oscaloosa, etc., Works v. Parkhurst, 54 Iowa 357. *Contra*, Phillips v. Covington, etc., R. Co., 2 Metc. (Ky.) 219.

[2] Denny Hotel Co. v. Schram, 6 Wash. 134, 32 Pac. Rep. 1002.

[3] Caley v. Philadelphia, etc., R. Co., 80 Pa. St. 363; Oscaloosa, etc., Works v. Parkhurst, 54 Iowa 357; Brand v. Lawrenceville, etc., R. Co., 77 Ga. 506; California, etc., Co. v. Russell, 88 Cal. 277.

[4] Salem, etc., Corp. v. Ropes, 9 Pick. 187; California, etc., Co. v. Russell, 88 Cal. 277, 26 Pac. Rep. 105; State v. Smith, 18 Vt. 266, 284.

[5] Brand v. Railroad Co., 77 Ga. 506; Oscaloosa, etc., Works v. Parkhurst, 54 Iowa 357, 6 N. W. Rep. 547; Southern, etc., Co. v. Russell, 88 Cal. 277.

[6] Hudson, etc., Co. v. Tower, 156 Mass. 82, 30 N. E. Rep. 465, 161 Mass. 10, 36 N. E. Rep. 680; Muncie, etc., Co. v. Green, 143 Pa. St. 269, 13 Atl. Rep. 747; Cook v. Chittenden, 25 Fed. Rep. 544; Holt v. Winfield Bank, 25 Fed. Rep. 812; Marysville, etc., Co. v. Johnson, 93 Cal. 538; Lewis v. Mill Co. (Texas Civ. App.), 23 S. W. Rep. 338; Plank, etc., Co. v. Burkhard, 87 Mich. 182, 49 N. W. Rep. 562.

[7] Wallace v. Townsend, 43 Ohio St. 537, 3 N. E. Rep. 601.

[8] Richelieu, etc., Co. v. Int., etc., Co., 140 Ill. 248. See Minneapolis, etc., Co. v. Davis, 40 Minn. 110.

tion are executed and officers elected, oral notice to the president at any time before the completion of the incorporation is sufficient.[1] Notice to the promoters' agent who secured the sub-

[1] In Hudson,etc.,Co.v.Tower(Mass.) 36 N. E. Rep. 680, the court, by Allen, J., said: "The plaintiff's requests for instructions raised no question on this point, but asked the court to rule that, 'in order to constitute a valid withdrawal, the defendants must do some act, or make some unequivocal or unconditional statement, to the proper officer or officers of the associates, which shall amount to a public withdrawal from said contract.' The instructions were given with reference to this request, and, as we understand them, they amounted to this: that Mr. Tower, having been chosen as president, and acting for the associates, was, on August 31st, a proper officer to be notified by the defendants of their withdrawal. We think this instruction was right. No instruction was asked at the trial that, in order to withdraw from the associates, notice must be given to all of them individually, or at a meeting of the associates. The plaintiff only contended that the notice must be given to the proper officer or officers. And it would plainly be impracticable to require a direct personal notice to them all. The right to withdraw would be nugatory if this were necessary. A subscriber who has a right to withdraw may not know, or have the means of knowing, who all of his associates are, or where they live. If he does know, they may be many in number, and widely scattered, or some of them may be away on a journey. No general meeting of them may be called which he can attend without leaving the state. He need not wait for a meeting before giving his notice of withdrawal. It was indeed held, in an early case in England, that all of the other subscribers must not only have notice, but must actually consent, before one of the subscribers could withdraw. Canal Co. v. Raby, 2 Price (Ex.) 93. But now, in England as well as here, no such consent is necessary. If every one of the other subscribers should object, yet it is the right of a subscriber to withdraw before the corporation is formed. It is merely a question of giving due notice of his withdrawal. And in England it is not intimated in any modern case, so far as our examination has gone, that notice must be given to all the other subscribers, or to a meeting of subscribers. The retraction has usually been made to the same person to whom the application for shares was made. See Lindl. Partn. 99-105, and numerous cases cited.

"In this country, no case has been cited, and we have found none, discussing the question what notice of withdrawal will be sufficient. In some cases, no attempt to withdraw was made till after the corporation was formed. See, for examples, Association v. Walker, 83 Mich. 386, 47 N. W. Rep. 338; Richelieu, etc., Co. v. International, etc., Co., 140 Ill. 248, 29 N. E. Rep. 1044; Shoe Co. v. Hoit, 56 N. H. 548; Shober v. Association, 68 Pa. St. 429. It is said in Cartwright v. Dickinson, 88 Tenn. 476, 12 S. W. Rep. 1030: 'Before the organization of the corporation and acceptance of the subscription, * * * the promoters might perhaps agree to release a subscriber by substituting other names for his.' This goes on the idea that the subscriber has not an absolute right to withdraw, and

scription of the intention to withdraw, and a request that the subscriber's name be dropped from the subscription paper, which facts are communicated to the subscribers at one of their meetings before organization, is sufficient.[1] There can be no withdrawal after the incorporation is completed.

§ 366. **Implied agreement to pay for shares.**—A subscription for shares in a corporation having capital stock implies a promise to pay for them, which will sustain an action to collect without proof of any particular consideration.[2] This rule applies as well to subscriptions taken before as after incorpo-

that somebody's assent is necessary. In Tavern Co. v. Burkhard, 87 Mich. 182, 49 N. W. Rep. 562, the subscriber apparently made known his refusal to the persons who brought a second paper to be signed by him, and it was held to be sufficient; but the proper mode of giving such notice is not discussed, and the court incidentally remarked that 'the corporators well knew, when the company was organized, * * * that the defendants expressly repudiated the whole arrangement.' It is held that the death of a subscriber before the formation of the corporation is a revocation of the subscription. Phipps v. Jones, 20 Pa. St. 260; Wallace v. Townsend, 43 Ohio St. 537, 3 N. E. Rep. 601; Pratt v. Trustees, 93 Ill. 475; Railway Co. v. Wilkerson, 83 Mo. 235. Insanity is also held to be a revocation in Beach v. Methodist, etc., Church, 96 Ill. 177. Death is a public fact, of which all the world must take notice, though the above decisions were not put on that ground (Marlett v. Jackman, 3 Allen 287), but insanity is not. In most of the cases where the right of withdrawal of a subscription has been held to exist, there is nothing to show that all the other subscribers were notified, and there has been no question as to the sufficiency of the mode in which the withdrawal was made. See, in addition to the cases above cited, Auburn Bolt & Nut Works v. Schultz, 143 Pa. St. 256, 22 Atl. Rep. 904; Engine Co. v. Green, 143 Pa. St. 269, 13 Atl. Rep. 747; Garrett v. Railroad Co., 78 Pa. St. 465; Railroad Co. v. Echternacht, 21 Pa. St. 220. An offer of reward made by public proclamation may be withdrawn in the same manner, and the fact that a claimant of the reward was ignorant of the withdrawal of the offer is immaterial. Shuey v. United States, 92 U. S. 73. And, if not withdrawn by any express notice, a withdrawal is implied after the lapse of a considerable time. Loring v. Boston, 7 Metc. (Mass.) 409."

[1] Bryant's, etc., Co. v. Felt, 87 Me. 234, 33 L. R. A. 593, annotated.

[2] Upton v. Tribilcock, 91 U. S. 45; Busey v. Hooper, 35 Md. 15, 30; Fort Edward, etc., Co. v. Payne, 17 Barb. 567; N. Y. etc., Co. v. Martin, 13 Minn. 417; Walter A. Woods, etc., Co. v. Robbins, 56 Minn. 48, 57 N. W. Rep. 317; Penobscot, etc., R. Co. v. Dunn, 39 Me. 587; Nulton v. Clayton, 54 Iowa 425; Mansfield, etc., R. Co. v. Brown, 26 Ohio St. 223; Windsor, etc., Co. v. Tandy, 66 Vt. 248, 29 Atl. Rep. 248; Bavington v. Railroad Co., 34 Pa. St. 358; Buffalo, etc., Co. v. Dudley, 14 N. Y. 336.

ration,[1] and is supported by the weight of authority, although it has been held that the corporation can not maintain an action unless the preliminary subscription ran to the corporation.[2] It may, however, recover damages for the refusal to take the stock.[3] A remedy by forfeiture, if it is meant to be a mere security reserved by the charter or statute to the corporation, is merely cumulative and does not affect the personal liability of the stockholder to pay for the stock.[4] But if it is meant to be a true forfeiture, so that the stock is reclaimed by the corporation, the shareholder is no longer liable.[5]

§ 367. **The New England rule.**—In some of the New England states it is held that a subscriber can not be required to pay for the stock unless he has expressly promised to pay, or the charter expressly obligates him to do so.[6] The rule in New Hampshire is thus stated by Mr. Justice Eastman: "Where a party makes an express promise to pay the assessments he is answerable to the corporation upon such promise for all legal assessments, and may be compelled to its performance by an action at law, before resorting to a sale of the shares. It is a personal undertaking beyond the terms of the charter. Where, on the other hand, he only agrees to take a specified number of shares, without promising expressly to pay assessments, then resort must first be had to a sale of the shares to pay the assessments before an action at law can be maintained. His agreement merely to take the shares is an agreement upon the faith of the charter, and by it alone is he to be governed so far

[1] Minneapolis, etc., Co. v. Crevier, 39 Minn. 417; Minneapolis, etc., Co. v. Davis, 40 Minn. 110; Richelieu, etc., Co. v. International, etc., Co., 140 Ill. 248, 29 N. E. Rep. 1044.

[2] Lake Ontario, etc., R. Co. v. Curtiss, 80 N. Y. 219. But see San Joaquin, etc., Co. v. West, 94 Cal. 399, Wilgus' Cases.

[3] Quick v. Lemon, 105 Ill. 578.

[4] Hartford, etc., R. Co. v. Kennedy, 12 Conn. 499.

[5] Mills v. Stewart, 41 N. Y. 384; Rutland, etc., R. Co. v. Thrall, 35 Vt. 536; Carson v. Mining Co., 5 Mich. 288.

[6] Mechanics', etc., Co. v. Hall, 121 Mass. 272; Worcester, etc., Co. v. Willard, 5 Mass. 80; Atlantic Cotton Mills v. Abbott, 9 Cush. 423; Katama, etc., Co. v. Holley, 129 Mass. 540; Kennebec, etc., R. Co. v. Kendall, 31 Maine 470; Belfast, etc., R. Co. v. Moore, 60 Maine 561; Penobscot, etc., R. Co. v. Dunn, 39 Maine 587. But see Windsor, etc., Co. v. Tandy, 66 Vt. 248.

as his shares are to be affected. He takes them upon the conditions and law of the charter. They exist only by virtue of the charter, and are to be governed by the provisions therein contained."[1]

§ 368. **Premature contract by corporation—Effect upon subscription.**—The liability of a subscriber for an assessment does not, as a rule, arise until the corporation is sufficiently organized and qualified by the subscription of the required capital stock to enter upon the general business.[2] But a premature and void contract made by a corporation before the amount of capital stock required by the statute has been paid in will not release the subscriber. A corporation organized to construct water-works entered into a contract for the construction of the works before the amount of capital stock required by the law before it could begin business was subscribed. In an action brought by the corporation against a subscriber to collect an assessment, the court said: "In the formation of a private civil corporation there are two classes of contracts to be considered. One is the contract which the corporators or promoters make each with all the others, in order to bring the corporation into existence, of which a subscription to the capital stock is an example, and which necessarily antedates its completed existence. These are the organizing contracts. The other class is the contract which the corporation itself after it comes into complete existence makes with third persons. Both these classes of contracts depend upon the provisions of the charter; and it is usual that the charter of every corporation contains provisions relating to each. The organizing contracts are made primarily by each of the subscribers with each of the others. They are, also, in a sense, made with the corporation. But the making of them is not an exercise of any of the powers or privileges granted to the corporation, because they are the steps necessary to be taken before the corporation is qualified to exercise any of the powers or privileges granted to it. It needs hardly to be said that there must be a full com-

[1] New Hampshire, etc., R. Co. v. Johnson, 30 N. H. 390.

[2] Anvil, etc., Co. v. Sherman, 74 Wis. 226, 4 L. R. A. 232.

pliance with all the charter provisions relating to the organizing contracts before the corporation comes into such a legal existence as to be able to make contracts with third persons at all. Until these preliminary steps have been taken there is no legal person in being capable of exercising any power or privilege whatever. It is obvious enough that any omission or failure to complete the organization would affect any contract with a third person. How any premature contract with a third person could interrupt or hinder the organization is not so plain. If any organizing contract was by its terms conditioned that no such contract should be entered into, or if it was so made conditional by the terms of the charter, then it would appear. The contract of subscription, signed by the defendant, is not by its terms conditioned upon anything relating to contracts which the plaintiff might make with third persons, unless the reference to it in the charter puts it in such a condition. * * * The defendant claims that that provision of the charter above quoted is such a condition by implication, because it forbids the plaintiff to exercise any of the granted privileges and powers until the required part of the capital stock should be paid in. It does not seem to us that this claim can be sustained. * * * The provision of the charter clearly forbade such a contract. Being forbidden, it was void.'"[1]

§ 369. **Effect of fraud upon the contract of subscription.**— The general rule is that whenever the agent of the corporation duly authorized by the corporation to procure subscriptions to its capital stock induces persons to become subscribers to such capital stock by fraudulent representations or concealments, the person so defrauded will be entitled to claim of the corporation a rescission of the contract in the same manner as though the question had arisen between two natural persons, —whenever the question arises between the contracting parties, and the rights of third persons are not involved.[2] Or,

[1] Naugatuck Water v. Nichols, 58 Conn. 403, 8 L. R. A. 637.

[2] Thomps. Corp., § 1361; French v. Ryan, 104 Mich. 625; Jewett v. Valley R. Co., 34 Ohio St. 601; Occidental, etc., Co. v. Ganzhorn, 2 Mo. App. 205; Prov., etc., Co. v. Brown, 9 U. C. C. P. 286. A transferee of shares can not be relieved against fraud which induced the subscription by his transferrer. Langer's Case, 37 L. J. Ch. N. S. 292.

as stated in the language of Lord Romilly, "contracts of this description between an individual and a company, so far as misrepresentation or suppression of truth is concerned, are to be treated like contracts between any two individuals. If one man makes a false statement which misleads another, the way this is to be treated affords an example of the way in which a contract is to be treated where a company makes a false statement which misleads an individual."[1]

§ 370. **The English doctrine.**—The early English cases held that a subscriber could not escape liability as a contributory by showing that he was induced to subscribe for the shares by the false or fraudulent representations or concealments of the agent of the corporation. In order to be relieved from his contract it was necessary for him to show that the fraud was the fraud of the company itself.[2] But "whilst the results reached in these cases are no doubt in conformity with the general current of the authorities, English and American, there is now little room to doubt that the ground taken by Lord Romilly and other English equity judges that a corporation is not bound by the fraud of its agent, is, where no other rights are concerned than those of the company and the person defrauded, fundamentally wrong; because as corporations and joint stock companies can only act through agents, it gives them an immunity in the commission of fraud not extended to individuals."[3] But the English courts in the leading case of Oakes v. Turquand[4] adopted the rule that where a person was induced to subscribe for stock in a corporation by the fraudulent representations of the directors of the corporation the contract was voidable, and although the persons who by their fraud induced it might not enforce it, yet other persons may in consequence of it acquire rights and interests which may be enforced against the party who has been so induced to enter into it; that a person who has been by such fraudulent representations induced to enter into a contract to purchase shares in a company may have the same rescinded within a reasonable time,

[1] Directors v. Kisch, L. R. 2 H. L. 99.

[2] Ex parte Nicol, 5 Jur. N. S. 205; Ayres' Case, 25 Beav. 513.

[3] Thomps. Corp., § 1362.

[4] Oakes v. Turquand & Harding, L. R. 2 H. L. 325.

but that he can not relieve himself from liability to contribute to the payment of its debts on the ground that he has been ignorant of something which with proper diligence he might have known. As between the company and the member, the member may have a good legal or equitable defense, but he may still be called upon to contribute to the assets of the company for the purpose of satisfying the corporate creditors.[1]

§ 371. **The contract voidable merely—Authority of agent.**—A contract which a person has been induced to enter into by fraud is voidable only at his election.[2] Before there can be a rescission on the ground of fraudulent representations by the agent of the corporation, the fact of agency must be shown, but it is not necessary that the agent should have had express authority to make the representation or commit the fraud. "That a person professing to act as the agent of another does so wholly without authority, or transcends the authority actually conferred upon him by the principal, is no reason for enforcing the contract against the other party when obtained from him by false and fraudulent representations."[3] The corporation is not of course responsible for representations made by the person who assumes to represent it, when they are entirely beyond the scope of his employment and the results have not been accepted or ratified by the corporation. In a Pennsylvania case the court said: "The principle of the cases would seem to be this: that, where representations made by an agent to procure subscriptions are a part of a scheme of fraud participated in by the officers authorized to manage its affairs, or where they are such that the agent may reasonably be presumed by the subscriber to have the authority of the corporation to make them, his representations may be given in evidence to show the fraud by means of which the subscription

[1] See summary of this case Thomp. Corp., § 1363.

[2] Bosher v. Richmond, etc., Co., 89 Va. 455, 37 Am. St. Rep. 879; Wesiger v. Richmond, etc., Co., 90 Va. 795; Upton v. Englehart, 3 Dill. (C. C.) 496; Farrar v. Walker, 3 Dill. (C.C.) 506.

[3] Crump v. United States, etc., Co., 7 Grat. (Va.) 352, 56 Am. Dec. 116; Waldo v. Chicago, etc., R. Co., 14 Wis. 625; Tradesmen's Nat'l Bank v. Looney, 99 Tenn. 278, 38 L. R. A. 837.

was procured. But when there is no reasonable presumption of authority and no actual authority to make them, the corporation should not be prejudiced by the unauthorized acts of the agent. Hence, when the representation of the agent is contrary to the interest and duty of the corporation, as that he will release, or has authority to release, the subscription he is taking, it is not a reasonable presumption that he has such authority, and a subscriber on such terms would be *particeps criminis* and held to all the responsibility of a bona fide subscriber."[1] A corporation is not responsible for fraudulent representations made by its president in selling stock fraudulently issued by the president, of which he was the owner at the time of the representations.[2]

§ 372. **Fraudulent representations by promoters.**—Before a subscriber can have a contract of subscription rescinded for fraudulent representations, he must make it appear that the representations were made by some one having authority to represent the corporation. As a promoter is not the agent of the corporation not yet in being, it follows that the corporation is not bound by his representations or promises.[3] In order to make the corporation liable in damages to subscribers, who have been led to take shares by false and fraudulent representations it must be shown that such representations were made by agents of the corporation acting within the scope of their authority. In an action for damages on the ground of fraudulent representations, it is essential to prove knowledge by the defendant or his agent of the falsity of the statement alleged to have deceived the plaintiff. As a corporation can not have agents before it exists, it follows that it is not liable in damages for misrepresentations made by its promoters through prospectuses or otherwise before it comes into existence.[4] Not having made the representations itself or by its agents, it is

[1] Custar v. Titusville, etc., Co., 63 Pa. St. 381. See, also, Robinson v. Pittsburgh, etc., R. Co., 32 Pa. St. 334, 72 Am. Dec. 792.

[2] Dunn v. State Bank, 59 Minn. 221, 61 N. W. Rep. 27.

[3] Joy v. Manion, 28 Mo. App. 55.

[4] Miller v. Wild Cat, etc., Co., 57 Ind. 241; Kennedy v. McKay, 43 N. J. L. 288; Presby v. Parker, 56 N. H. 409.

not responsible for them. But the promoters may, in fact, after its formation, act as its agents in procuring subscriptions for shares.[1]

The fraud of promoters in procuring a subscription to the stock of a corporation is not a defense to an assessment on the stock by the corporation after the subscriber has carried out his contract and united with others in forming a corporation. His remedy is then restricted to an action against the person making the representations.[2] The defendant united with others for the purpose of forming a corporation, and a preliminary subscription was obtained by a citizens' committee, which was chosen at a public meeting. The subscription was followed by the adoption and signing of articles of incorporation. Those who subscribed the articles became the stockholders. The court said: "The proposition that such stockholder could charge the association with fraud because he was misled by the fraud of interested persons is suggestive of troublesome results. If this can be done, and the stockholder thereby escape payment for this stock, other stockholders, innocent of the fraud, would find their responsibilities proportionately increased, and the burdens of the concern would be shifted to those members who were unable to show that they became such through the fraud of others. There would be little stability to corporations and little safety to stockholders if this doctrine should be sustained. In this case there not only was not a corporation in existence to be a principal, but the facts set up in the notice do not show that there was an agent of the corporation. The promoters were persons who represented the meeting, or possibly themselves or some prospective stockholder, who, for purposes of his own, desired to see the corporation organized. They can not be said to be agents of the corporation in any sense."[3]

False representations as to the value of property, made by the representatives of a syndicate, and not the corporation, is

[1] Alger, Promoters and the Promotion of Corps., § 171.

[2] See Franey v. Warner, 96 Wis. 222; Getty v. Devlin, 70 N. Y. 504.

[3] St. John's, etc., Co. v. Munger, 106 Mich. 90, 29 L. R. A. 63, 64 N. W. Rep. 3.

no defense to a promissory note given for the stock of the syndicate which was to purchase the property of the corporation, and which was transferred to the vendor corporation in payment for the property.[1]

§ 373. **What frauds will vitiate.**—In order to avoid a contract of subscription on the ground of fraud, the party must show that a false representation or wilful concealment of a material fact was made with an intent to deceive; and that the statements were relied upon and actually deceived him to his injury.[2] In a case where the nature of such misrepresentations was carefully considered, Lord Romilly said:[3] "The basis of this as well as of most of the great principles on which the system of equity is founded is the enforcement of a careful adherence to truth in the dealings of mankind. This principle is universal in its application to cases of contract. It affects not merely the parties to the agreement, but also those who induce others to enter into it. It applies not merely to cases where the statements were known to be false by those who made them, but to cases where statements, false in fact, were made by parties who believed them to be true, if in the due discharge of their duty they ought to have known, or if they had formerly known and ought to have remembered the facts which negatived the representation made. * * * With respect to the character or nature of the misrepresentation itself, it is clear that it may be positive or negative; that it may consist as much in the suppression of what is true as in the assertion of what is false; and it is almost needless to add, that it must appear that the person deceived entered into the contract on the faith of it." It is not necessary, at least in equity, that the fraud should have been willful. This rule

[1] Tradesmen's Nat'l Bank v. Looney, 99 Tenn. 278, 38 L. R. A. 837. In Hunter v. French, etc., Co., 96 Iowa 573, the subscription seems to have been rescinded because of the fraudulent representations of the promoters.

[2] Connecticut, etc., R. Co. v. Bailey, 24 Vt. 465; Goodrich v. Reynolds, etc., Co., 31 Ill. 490. The fraud must be affirmatively shown. First Nat'l Bank v. Hurford, 29 Iowa 579; Wenstrom, etc., Co. v. Purnell, 75 Md. 113.

[3] Pulsford v. Richards, 22 L. J. Ch. 559. See, also, Salem, etc., Corp. v. Ropes, 9 Pick. (Mass.) 187, 19 Am. Dec. 363; Goodrich v. Reynolds, 31 Ill. 490, 83 Am. Dec. 240.

applies in an action for rescission; but if the action is for deceit against the persons who were guilty of the fraud, it is necessary to show guilty knowledge. In an action brought on calls, where the defense was fraud in procuring the subscription, the court said:[1] "The defendant, no doubt, is bound to make out a case of moral fraud, but that does not necessarily involve a knowledge of falsehood. It is a fraud to state things which are untrue for the purpose of gain; whether the statement is made with a knowledge of their untruth or with a reckless disregard of whether they are true or false, if it be with the intention of misleading another. To state things knowing them to be false, or not knowing whether they are true or false, and careless whether they are true or not, is equally fraudulent. Utter carelessness of truth, where the interests of others is concerned, is evidence of fraud." A representation as to matters of which the subscriber is bound to take notice, as of a matter of law, the extent of the corporate powers and the like is no defense to an action on the contract of subscription.[2] So it is no defense to an action based on fraudulent representations that the subscriber might have discovered the truth had he made proper inquiry.[3]

§ 374. **Expressions of belief or opinion.**—It is well settled that oral statements of matters of opinion, intention and belief are not such representations as will authorize a court to set aside a contract of subscription.[4] But "we will not say that a case might not arise where a statement on the part of

[1] Glamorganshire, etc., Co. v. Irvine, 4 Fost. & Fin. 947.

[2] Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; Russell v. Alabama, etc., R. Co., 94 Ga. 510. Matters of law. Clem v. Newcastle, etc., R. Co., 9 Ind. 488, 68 Am. Dec. 653; Upton v. Tribilcock, 91 U. S. 45. Misstatement as to amount of capital that has been subscribed, and of the amount paid for property. Kent v. Freeland, etc., Co., L. R. 4 Eq. 588; Wanstrom, etc., Co. v. Purnell, 75 Md. 113. For illustrations of fraudulent statements see the cases collected in a note to Fear v. Bartlett, 33 L. R. A. 721.

[3] Directors v. Kisch, L. R. 2 H. L. 99. But see Mullen v. Beech Grove Park, 64 Ind. 202.

[4] Richelieu, etc., Co. v. International, etc., Co., 140 Ill. 248, 29 N. E. Rep. 1044; Armstrong v. Karshner, 47 Ohio St. 276, 24 N. E. Rep. 897; Jefferson v. Hewitt, 95 Cal. 535.

the agent as to the pecuniary condition and prospects of his corporation would not avoid a subscription, but it must be a case where both the falsity and the fraud of such representation are clearly shown, and where it is manifest that the condition of the enterprise constituted a material inducement to the subscription. To hold that every subscription to an inchoate undertaking like this can be avoided because some enthusiastic or reckless agent has boasted of its resources or prophesied its speedy completion would be to nullify perhaps the majority of such contracts. To escape from a subscription on this ground, several things must concur. It must be shown that the statement was not uttered as an opinion but as an ascertained and existing fact. It must not only be false in fact, but must also be either known to be so by the party uttering it, or his position must be one that made it his duty to know the truth. The resisting subscriber must show that he acted upon such statement; that his position was such as warranted him in so acting, and that the statement was as to a fact material to the question of his subscription. Even with these limitations it will not avail if the representations are as to matters controlled by the charter, and as to which the subscriber is legally bound to know that the agent has no right to make representations inconsistent therewith.''[1]

The representation must be as to a matter of fact and not of belief of a present fact or condition or of expectation of the future.[2] So rescission will not be allowed because of representations as to the legal rights or powers of the corporation, such as the right of a railway company to construct a certain road.[3] A subscription made after the organization of the corporation, which was induced by false and fraudulent representations as to the purposes and powers of the corporation will not be

[1] Selma, etc., R. Co. v. Anderson, 51 Miss. 829; Wight v. Shelby, etc., R. Co., 16 B. Mon. (Ky.) 4; Ellson v. M. & O. R. Co., 36 Miss. 572; Montgomery, etc., R. Co. v. Matthews, 77 Ala. 357, 54 Am. Rep. 60.

[2] Columbia, etc., Co. v. Dixon, 46 Minn. 463.

[3] Jackson v. Stockbridge, 29 Tex. 394, 94 Am. Dec. 290; Bish v. Bradford, 17 Ind. 490; Piscataqua, etc., Co. v. Jones, 39 N. H. 491.

rescinded, as the subscriber is bound by knowledge of the provisions of the charter.[1]

§ 375. **Remedies of defrauded stockholders.**—A person who is induced by fraudulent representations or concealments to subscribe for shares in a corporation is entitled, if he acts promptly, to a rescission of the contract,[2] or an injunction to restrain calls,[3] or he may assert the facts as a defense to a suit on an assessment,[4] or for a specific performance of the contract, or in an action for damages against the corporation.[5] The necessary elements of the plea of fraud, as stated by Thompson,[6] are:

1. A distinct allegation of the matter in which the fraudulent representation consisted.

2. That he used reasonable diligence to make himself acquainted with the matters of fact in respect to which the fraud is charged, and that within a reasonable time after discovering the facts he repudiated his contract and offered to surrender his certificate.

After rescinding the contract the defrauded subscriber may recover from the corporation the money which he has already paid under the contract.[7]

§ 376. **Rescission—Necessity for prompt action—Laches.**—A subscriber may have a contract of subscription which was induced by fraud rescinded and annulled, if he acts promptly and before the rights of creditors or subsequent stockholders have accrued. All the cases agree, however, that he must act

[1] Oil City, etc., Co. v. Porter, 99 Ky. 254.

[2] Waldo v. Chicago, etc., R. Co., 14 Wis. 625; Henderson v. Railway Co., 17 Tex. 560, 67 Am. Dec. 675.

[3] Reese River Co. v. Smith, L. R. 4 H. L. 64.

[4] Davis & Co. v. Dumont, 37 Iowa 47; Crump v. United States, etc., Co., 7 Grat. (Va.) 352, 56 Am. Dec. 116; Occidental, etc., Co. v. Ganzhorn, 2 Mo. App. 205; Provincial, etc., Co. v. Brown, 9 U. C. C. P. 286; Jewett v. Valley R. Co., 34 Ohio St. 601. It is a defense to an action on a note given for the subscription. French v. Ryan, 104 Mich. 625.

[5] Bosley v. National, etc., Co., 123 N. Y. 550.

[6] Thompson Corp., § 1431.

[7] Lare v. Westmoreland, etc., Co., 155 Pa. St. 33. May proceed by attachment against the corporation as for money had and received. Granger, etc., Co. v. Turner, 61 Ga. 561. But the money can not be recovered when the fraud was that of the promoter. Perry v. Hale, 143 Mass. 540.

with diligence in order to obtain a rescission.[1] As the contract is merely voidable it may be ratified, after which it can not be repudiated.[2] He can not wait until he sees whether the enterprise is going to be a failure or a success. "He can not say, 'I will abide by the company if successful, and I will leave the company if it fails,' and therefore, whenever a misrepresentation is made of which any one of the shareholders has notice and can take advantage of to avoid his contract with the company, it is his duty to determine at once whether he will depart from the company, or whether he will remain a member."[3]

§ 377. **Insolvency—The rights of creditors—English doctrine.**—As to the right of a subscriber to have the contract rescinded after the corporation has become insolvent, or third parties have become creditors of the corporation upon the faith of his name upon the register of corporate books, the decisions are conflicting. It is the settled law in England that the insolvency of the corporation cuts off the right of the subscriber to a rescission without reference to his laches. He must act while the corporation is a going concern, or his remedy is lost.[4] Thus Lord Bramwell said: "Where a company is shown by a winding-up to be insolvent, and where the remedies of the creditors who have trusted the company upon the strength of the uncalled capital, and the names upon the register, would be interfered with by the withdrawal of members, the power to rescind the contract to take shares is gone."[5]

"I take it to be perfectly clear," said Vice-Chancellor Malins,[6] "since the case of Oakes v. Turquand, that where there is a question of whether a man is a contributory or not, no misconduct of the company or false representation or mis-

[1] Oakes v. Turquand, L. R. 2 H. L. 325. See note to Fear v. Bartlett, 33 L. R. A. 721.

[2] City Bank v. Bartlett, 71 Ga. 797.

[3] Lord Romilly in Ashley's Case, L. R. 9 Eq. 263; Ogilvie v. Knox, etc., Co., 22 How. (U. S.) 380.

[4] Oakes v. Turquand, L. R. 2 H. L. 325; Wright's Case, L. R. 12 Eq. 331; Burgess's Case, L. R. 15 Ch. Div. 507; Re Scottish, etc., Co., L. R. 23 Ch. Div. 413.

[5] Stone v. City and County Bank, 3 C. P. Div. 282.

[6] Pugh and Sharman's Case, L. R. 13 Eq. 566. See, also, Henderson v. Royal Brit. Bank, 7 El. & Bl. 356.

representation, made by them as a means of inducing him to take shares, will relieve him from bearing the responsibility which he at all events holds to creditors, whatever effect it may have between himself and other shareholders."

§ 378. **Rule in the United States.**—There is no established rule in this country which cuts off the shareholder from claiming a rescission after the commencement of winding up proceedings, without reference to the diligence he has exercised in discovering his rights, and repudiating his contract on account of the fraud practiced upon him.[1] In many cases the relief has been denied after insolvency, but the decisions ordinarily turn upon the question of estoppel or laches. It is admitted that if the subscriber acts promptly, he may have the contract rescinded at any time before the corporation becomes insolvent, and the rights of creditors attach.[2] But, after the corporation has become insolvent, and has gone into liquidation and is making calls to satisfy the claims of creditors, it is frequently held that it is too late for one whose name had appeared as a stockholder to repudiate the contract and escape liability on the ground that his subscription was obtained by fraud.[3] In all these cases the evidence showed that there had either been lack of diligence on the part of the stockholder in discovering the fraud of which he complained, or unreasonable delay in asserting his rights after the discovery of the fraud, or active participation in the management of the corporation, or that debts had been contracted by the corporation subsequent to the subscription, which either gave to corporate creditors

[1] See Thomp. Corp., § 1449.

[2] Marten v. Burns, etc., Co., 99 Cal. 355; Dunn v. State Bank (Minn.), 61 N. W. Rep. 27. If the rights of innocent third persons require that the subscription be enforced, the subscriber will not be permitted to repudiate his liability. Dettra v. Kestner, 147 Pa. St. 566.

[3] Upton v. Tribilcock, 91 U.S. 45; Bissell v. Heath, 98 Mich. 472, 57 N. W. Rep. 585; Duffield v. Barnum, etc., Co., 64 Mich. 293; Turner v. Grangers, etc., Co., 65 Ga. 649, 38 Am. Rep. 801; Howard v. Turner, 155 Pa. St. 349; Hurd v. Kelley, 78 N. Y. 588, 34 Am. Rep. 567; Mathis v. Pridham, 1 Tex. Civ. App. 58, 20 S. W. Rep. 1015; Howard v. Glenn (Ga.), 11 S. E. Rep. 610; Upton v. Tribilcock, 91 U. S. 45. See Upton v. Hansborough, 3 Biss. (C. C.) 417.

superior equitable rights,[1] or estopped the shareholder as against the corporate creditor from asserting that he was not a shareholder. Thus, an act done after the discovery of the fraud which is inconsistent with disaffirmance is a waiver of the right, at least in favor of creditors.[2] A subscriber who has served as a director of the corporation can not thereafter assert the invalidity of his subscription for stock.[3] One who, after discovery of the fact that his subscription was induced by fraud, remains silent in the hope of receiving a large dividend in the near future, can not after failing to receive it withdraw from the company.[4] One who, after notice of the fraud, participates in negotiations looking to reorganization can not thereafter rescind as against creditors.[5] Acting as a shareholder, or receiving a benefit from the shares after notice of fraud will estop the subscriber from rescinding the contract.[6] One who is a party to the fraud can not, of course, be relieved from its consequences.[7] But the payment of money to save money already paid on a subscription which has been repudiated for fraud will not necessarily amount to an affirmance of the subscription.[8] Mere delay may be sufficient to defeat the right to rescind. The application for relief must be made at the earliest possible moment after discovery of the fraud.[9] The laches does not begin to run until the subscriber is chargeable with notice of the fraud.[10] A subscriber who allows his name

[1] See Turner v. Grangers, etc., Co., 65 Ga. 649, 38 Am. Rep. 801.

[2] Weisiger v. Richmond, etc., Co., 90 Va. 795.

[3] American, etc., Assn. v. Rainbolt (Neb.), 67 N. W. Rep. 493.

[4] Ogilvie v. Knox, etc., Co., 22 How. (U. S.) 380.

[5] Howard v. Turner, 155 Pa. St. 349.

[6] City Bank v. Bartlett, 71 Ga. 797; Nicols' Case, 3 DeG. & J. 387.

[7] Litchfield Bank v Church, 29 Conn. 137; Southern, etc., R. Co. v. Hixon, 5 Ind. 165; Schaeffer v. Missouri, etc., Co., 46 Mo. 248.

[8] Fear v. Bartlett, 81 Md. 435.

[9] In re London, etc., Co. (Wallace's Case), L. R. 24 Ch. Div. 149. Delay of two months is fatal, Ogilvie v. Currie, 37 L. J. N. S. 541; six months, Ex parte Hale, 55 L. T. N. S. 670, and see Upton v. Englehart, 3 Dill. (C. C.) 496; Farrar v. Walker, 3 Dill. (C. C.) 506, note; delay of three years, Upton v. Tribilcock, 91 U. S. 45; seven years, Dynes v. Shaffer, 19 Ind. 165; Cedar Rapids, etc., Co. v. Butler, 83 Iowa 124.

[10] Virginia Land Co. v. Haupt, 90 Va. 533, 44 Am. St. Rep. 939, note. See notes, 3 Am. St. Rep. 797; note, 9 Am. Dec. 96, and note, 84 Am. Dec. 401.

to remain on the books of the corporation for years and receives dividends, which he does not offer to return, can not have the contract rescinded on the ground of fraud.[1]

§ 379. **Right to rescind after insolvency continued.**— The question whether a stockholder should be permitted to rescind his subscription, on the ground of fraud, after the insolvency of the corporation, is attended with much doubt and difficulty because of the peculiar relations which a shareholder sustains to the creditors of the corporation. Judge Dillon, in discussing the question,[2] suggested that the rigid English rule was influenced, in a measure, by the provision of the companies act,[3] which requires a "register of stockholders," to which the public has access. As no similar register is kept in this country, the English decisions, which hold that the commencement of proceedings to wind up a corporation is a bar to a suit for rescission, are not strictly applicable in this country. "I am inclined to the opinion that if a company has fraudulently misrepresented or concealed material facts, and thus drawn an innocent person into the purchase of stock, he at the time being guilty of no want of reasonable caution and judgment, and afterwards guilty of no laches in discovering the fraud, and he thereupon, without delay, notifies the company that he repudiates the contract, and offers to rescind the purchase, these facts concurring, I am inclined to the opinion that the bankruptcy of the company subsequently happening will not enable the assignee to insist that the purchase of stock is binding upon him."

In a recent case it was held that the insolvency of the corporation will not prevent the cancellation of a stock subscription for fraud if the subscriber acted with due diligence in discovering the fraud and repudiating the subscription and no considerable amount of indebtedness was contracted after the subscription was made. The question of due diligence is for the jury. "There are obvious reasons," said Judge Thayer,[4] "why

[1] Bissell v. Heath, 98 Mich. 472.

[2] Upton v. Englehart, 3 Dill. (C. C.) 496.

[3] 25 and 26 Vict. Ch. 89.

[4] Newton Nat'l Bank v. Newbegin, 20 C. C. A. 339, 74 Fed. Rep. 135, 33

a shareholder of a corporation should not be released from his subscription to its capital stock after the insolvency of the company, and particularly after a proceeding has been inaugurated to liquidate its affairs, unless the case is one in which the stockholder has exercised due diligence and in which no facts exist upon which corporate creditors can reasonably predicate an estoppel. When a corporation becomes bankrupt, the temptation to lay aside the garb of a stockholder and assume the role of a creditor is very strong, and all attempts of that kind should be viewed with suspicion. If a considerable period of time has elapsed since the subscription was made; if the subscriber has actively participated in the management of the affairs of the corporation, if there has been any want of diligence on the part of the stockholder, either in discovering the alleged fraud or in taking steps to rescind when the fraud was discovered, and above all if any considerable amount of indebtedness has been created since the subscription was made, which is outstanding and unpaid; in all of these cases the right to rescind should be denied, where the attempt is not made until the corporation becomes insolvent. But if none of these conditions exist and the proof of the alleged fraud is clear, we think that a stockholder should be permitted to rescind his subscription as well after as before the company ceases to be a going concern. There is some force, doubtless, in the view which has sometimes been taken by eminent judges, that when a person has been inveigled into making a stock subscription by representations that were clearly false and fraudulent, he should be entitled to rescind his subscription, even after the insolvency of the company, under the same circumstances that would entitle him to rescind a contract of a different nature; that is to say, by proof of due diligence in discovering the fraud, and of

L. R. A. 727, annotated. To the same effect see Dorsey Match Co. v. McCaffrey, 139 Ind. 545; Stuffelbeam v. De Lashmutt, 83 Fed. Rep. 449. In Martin v. South Salem, etc., Co., 94 Va. 28, it was held that there could be no rescission after the rights of bona fide creditors had intervened or the corporation stopped payment and became actually insolvent, at least without showing diligence in discovering the fraud and repudiating the contract.

prompt action after its discovery.[1] The case in hand, however, does not require us to go to that length even if we felt so disposed."

§ 380. **Rights of rescission before insolvency of corporation.** —Where a subscription to the capital stock of a corporation was procured through the false and fraudulent representation of the corporation, and the subscriber, without laches or unreasonable delay in discovering the fraud and within a reasonable time after such discovery, and before the execution by the corporation of a deed conveying its property in trust for the benefit of its creditors, notified the president of the corporation that he repudiated the contract and refused to make any further payment on account of his subscription, such facts constitute a valid defense to an action by the trustee to recover from the subscriber the unpaid installments due upon his subscription. The court said:[2] "The defense is that the defendant was induced to become a shareholder upon the faith of certain representations set forth in a prospectus issued by the company, and that these representations were false and fraudulent, and that the defendant within a reasonable time after the discovery of the fraud, and before the execution of the deed of trust, repudiated the contract and refused to make any further payments on account of his subscription. * * * As against the company itself it is well settled that a shareholder may rescind a contract of subscription procured through the fraud of the company within a reasonable time after the discovery of the fraud. * * * This well settled rule applies with even greater strictness with regard to representations set forth in a prospectus issued by a company for the purpose of inviting

[1] See Upton v. Tribilcock, 91 U. S. 45; Duffield v. Wire Works, 64 Mich. 293; Florida Land, etc., Co. v. Merrill, 2 U. S. App. 434, 52 Fed. Rep. 77.

[2] Savage v. Bartlett, 78 Md. 561; Duffield v. Wire Works, 64 Mich. 293, by a divided court. In Upton v. Englehart, 3 Dill. C. C. 496, the defense was held defective because it did not "show that the defendant made use of reasonable diligence to make himself acquainted with the matters in respect to which the fraud is claimed, nor when or how he repudiated the contract."

persons to join in the undertaking; and although some allowance must be made for the manner in which the advantages which are likely to be enjoyed by the subscribers are described, yet as was said by the lord chancellor in the case to which we have just referred, 'no misstatement or concealment of any material facts or circumstances ought to be permitted.'" After reviewing many cases the court said: "We may also refer to Farrar v. Walker,[1] before Mr. Justice Miller on appeal to the circuit court, in which that learned judge recognizes in express terms the right of the defrauded shareholder to repudiate the contract and to repudiate it even after the insolvency of the company, if he has not had reasonable time in which to examine into the affairs of the company before the appointment of the assignee."

In a subsequent case upon practically the same facts, the Savage case was adhered to, and it was said that there was nothing in the decision in conflict with the theory that unpaid subscriptions are a trust fund for the benefit of creditors, when that theory was rightly understood. It could have no application until after the corporation became insolvent.[2]

§ 381. **Insolvency—Rule of diligence.**—In a Minnesota case the court, after stating that it was unnecessary to determine whether the subscriber is bound absolutely as between him and the creditors regardless of laches, or whether he is bound only when he has not been guilty of laches, said: "To say the least a very different rule of diligence is required as between him and the creditors than is required between him and the corporation. While there is no privity of contract between him and the creditors, and as a mere stockholder he is not an agent of the corporation, still he is to a considerable extent a member of the corporate family. He has a right while it is a going concern to inspect the books and investigate the affairs of the corporation. He has visitorial powers and duties which the creditor has not. He held himself out as a stockholder and it is to be presumed, after the lapse of time, that creditors

[1] Farrar v. Walker, 3 Dill. C. C. 506.

[2] Fear v. Bartlett, 81 Md. 435, 33 L. R. A. 721.

became such on the faith of his liability as a stockholder. Under these circumstances it is, to say the least, his duty to use a high degree of care and diligence to see that creditors are not misled and deceived by his conduct. What would constitute laches as between him and the creditors would not as between him and the corporation itself."[1]

§ 382. **Enforcement of subscription contracts by action.**—If a subscriber neglects or refuses to pay his subscription according to its terms, the corporation may maintain an action against him upon the contract. It is generally held that a subscription raises an implied promise to pay the assessments, although in the New England states it is held that an express promise is necessary. The insolvency of the corporation is no defense to an action to collect subscriptions.[2]

§ 383. **Calls.**—Before an assessment can be collected, it is ordinarily necessary that there shall be a call in due form. If the charter of a corporation or the contract of subscription makes the amount of the subscription payable at once or at a stated time, it is not necessary that the directors should make a formal call on the subscriber.[3] But when a formal call is made necessary by the charter, by-law or contract, it is a condition precedent to liability and no action can be maintained to collect an assessment until the call is made by the proper person and in the prescribed manner.[4] This rule applies when the charter or contract is silent, and when the time of payment is left to be determined by the board of directors. If there is no determination of the person or body by which calls shall be made, they must be made by the di-

[1] Dunn v. State Bank, 59 Minn. 221, 61 N. W. Rep. 27.

[2] Dill v. Wabash, etc., R. Co., 21 Ill. 90.

[3] Ruse v. Bromberg, 88 Ala. 619; Phœnix, etc., Co. v. Badger, 67 N. Y. 294.

[4] North, etc., R. Co. v. Spouleck, 88 Ga. 283; Glenn v. Howard, 65 Md. 40; Seymour v. Sturgess, 26 N. Y. 134; Spangler v. Railway Co., 21 Ill. 275. See Williams v. Taylor, 120 N. Y. 244. When the contract requires a call the corporation can not show an oral contract to the effect that there should be no call: Grosse, etc., v. I'Anson's Ex'rs, 43 N. J. L. 442. A subscriber can not question the necessity of a call. Chouteau, etc., Co. v. Floyd, 74 Mo. 286.

rectors.[1] They must act in their capacity as a legally constituted board,[2] and in the manner prescribed by the charter. It has been held a call can not be made by a *de facto* board of directors,[3] but there are several cases to the contrary.[4] If the charter or by-law provides that a call shall be made by a certain person or body, a call made in any other manner or by any other person is invalid.[5] In the absence of a special requirement, the manner of making the assessment is within the control of the board of directors, and it is only necessary that their acts shall be sufficient to clearly indicate their intention to render a part or all of the unpaid subscription due and payable.[6] A call may be made upon all subscribers for the purpose of raising money for preliminary expenses,[7] but thereafter no further calls can be made until the corporation is ready to begin business.[8] This may of course be changed by the terms of the contract of subscription or by the provisions of the charter. After a subscriber repudiates his subscription no call is necessary before proceeding to enforce the contract.[9] An unpaid subscription draws interest from the time the subscriber is in default. If a call is necessary, interest begins to run from the time fixed for the payment of the call.[10] Under a statute providing for calls on "giving such notice thereof as the by-laws may prescribe," a by-law prescribing such notice is a condition precedent to a valid call.[11] The directors may be required to make calls at the instance of creditors,[12] or a call may be made by the court.[13] A call for an assessment need

[1] Budd v. Multnomah, etc., R. Co., 15 Ore. 413. The directors can not delegate the power to make calls. Silver Hook Road v. Greene, 12 R. I. 164.

[2] People, etc., Co. v. Wescott, 14 Gray (Mass.) 440; Moses v. Tompkins, 84 Ala. 613.

[3] Moses v. Tompkins, 84 Ala. 613.

[4] Chandler v. Sheep, etc., Co. (Utah, 1897), 49 Pac. Rep. 535; Steinmetz v. Versailles, etc., Co., 57 Ind. 457; Macon, etc., R. Co. v. Vason, 57 Ga. 314.

[5] People's, etc., Co. v. Wescott, 14 Gray (Mass.) 440.

[6] Budd v. Multonomah, etc., Co., 15 Ore. 413.

[7] Salem Mill Dam Corp. v. Ropes, 9 Pick. (Mass.) 187, 19 Am. Dec. 363.

[8] Anvil, etc., Co. v. Sherman, 74 Wis. 226.

[9] Cass v. Railroad Co., 80 Pa. St. 31.

[10] Gould v. Onconta, 71 N. Y. 298.

[11] Germania, etc., Co. v. King, 94 Wis. 439, 36 L. R. A. 51.

[12] Germantown, etc., Co. v. Fitler, 60 Pa. St. 124; Scovill v. Thayer, 105 U. S. 143.

[13] Marston v. Deither, 49 Minn. 423.

not name the time, place or person to whom the payment is to be made, where the corporation has a place of business and an officer authorized .to receive money due it, as the time under such circumstances is on demand to such officer at such place of business.[1]

§ 384. **Calls—Uniformity—Demand.**—A valid call must operate uniformly upon all the shareholders, and require all to pay the same proportion at the same time.[2] But if some shareholders have already contributed more than others, it would be not only the right but the duty of the directors to make calls upon other shareholders in such amounts as to equalize the contributions of all.[3] No notice or demand is necessary, unless provided for by the charter or contract.[4] But when required it is a condition precedent to liability unless waived by the subscriber.[5] A general provision for notice requires actual notice, and in such case publication is not sufficient.[6] But actual notice, although not given in the manner provided by the by-laws, is always sufficient.[7]

§ 385. **Release of subscriber—By consent.**—After a valid contract for subscription to shares has been made the subscriber can not withdraw or be released from his obligations without the consent of the corporation and all the stockholders,[8] and not with such consent if there are corporate debts unpaid.[9] But, as already stated, an agreement to take shares in a corpo-

An assessment made under an order of court in another state is conclusive on the stockholders, although residents in another state and not served. Mutual, etc., Co. v. Phœnix, etc., Co. (Mich.), 34 L. R. A. 694, annotated; Glenn v. Liggett, 135 U. S. 533.

[1] Western, etc., Co. v. Des Moines Nat'l Bank, 103 Iowa 455; Distinguishing, In re Cawley & Co., L. R. 42 Ch. Div. 209; North, etc., R. Co. v. Spullock, 88 Ga. 283.

[2] Great Western, etc., Co. v. Burnham, 79 Wis. 47, 47 N. W. Rep. 373; Pike v. Railway Co., 68 Maine 445.

[3] Morawetz Priv. Corp., § 147.

[4] Heaston v. Railway Co., 16 Ind. 275.

[5] Rutland, etc., R. Co. v. Thrall, 35 Vt. 536.

[6] Lake Ontario, etc., R. Co. v. Mason, 16 N. Y. 451.

[7] Jones v. Sisson, 6 Gray 288.

[8] Selma, etc., R. Co. v. Tipton, 5 Ala. 787; Payne v. Bullard, 23 (1 Cushman 88) Miss. 88.

[9] Cartwright v. Dickinson, 88 Tenn. 476; Boutin v. Dement, 123 Ill. 143, 14

ration to be organized is a mere offer which may be withdrawn at any time before it is accepted.

§ 386. **Release by act of corporation.** — The mere mismanagement of the affairs of a corporation by its officers and agents will not enable a stockholder to withdraw and be released from his obligation,[1] nor is he released by the fact that the corporation has violated its charter, and thus subjected itself to a possible forfeiture at the suit of the state.[2] But if the right to amend or alter the charter is not reserved in such a way as to make it a part of the contract of subscription[3] an amendment which materially changes or enlarges the purposes of the corporation will release a subscriber who did not consent thereto.[4] It is generally held that in order to release a subscriber such alteration must be material, although much conflict exists as to what is a material amendment or alteration.[5] In some states it is held that if the alteration is of such a character as to facilitate the object for which the corporation was originally organized, and is thus for the benefit of the subscriber, he will not be released from his contract, although the alteration is a material one.[6] A radical and material amendment never accepted and which became inoperative will not release a subscriber.[7] The mere granting of additional privileges will not release a subscriber, although the effect is to increase the liabilities of the corporation.[8] When no rights of creditors are involved, a complete and final abandonment of the business of the corporation will release a subscriber from further liability on his subscription.[9] In such case it is necessary for the subscriber to allege and prove "a final abandon-

N. E. Rep. 62; Chouteau, etc., Co. v. Floyd, 74 Mo. 286; Potts v. Wallace, 146 U. S. 689.

[1] American, etc., Assn. v. Rainbolt (Neb.), 67 N. W. Rep. 193.

[2] Craven v. Mills Co., 120 Ind. 6, 21 N. E. Rep. 981; Taggart v. Railroad Co., 24 Md. 563.

[3] Proprietors Union Locks v. Towne, 1 N. H. 11; Hartford, etc., R. Co. v. Croswell, 5 Hill (N. Y.) 383.

[4] Buffalo, etc., R. Co. v. Dudley, 14 N. Y. 336; Armstrong v. Karshner, 47 Ohio St. 276, 24 N. E. Rep. 897.

[5] § 488; Maner v. Staples, 32 Minn. 284.

[6] § 486; Illinois, etc., R. Co. v. Zimmer, 20 Ill. 654; Hartford, etc., R. Co. v. Croswell, 5 Hill (N. Y.) 383.

[7] Chattanooga, etc., R. Co. v. Warthen, 98 Ga. 599.

[8] Gray v. Navigation Co., 2 Watts. & Sarg. 156.

[9] Phœnix, etc., Co. v. Badger, 67 N. Y. 294.

ment of the work by the company, and also that the payment was not necessary for satisfying any existing demand against the corporation."[1] The mere failure by a railroad corporation to complete its road or a non-user of a part of the road will not release a subscriber unless some provision of the contract of subscription is violated.[2] There may be a release by mere delay to organize the corporation and accepting the offer to take shares. A subscription for shares in a corporation to be organized can not be enforced by the corporation where the rights of creditors have not intervened where no notice of the organization of the corporation was given to the subscriber and no attempt was made to compel him to take the stock until more than two years after the organization was completed.[3] A subscriber can not be held liable when the corporation has issued its entire stock to other subscribers and received pay therefor.[4]

§ 387. **By forfeiture.**—A corporation has no inherent power to forfeit shares of stock, and thus release the subscriber from further liability on his subscription because he is in default in the payment of assessments.[5] The power of forfeiture does not exist unless it is conferred by the charter or general law, and a by-law providing for forfeiture which does not rest upon a charter provision is invalid.[6] "We must look to the charter," said Mr. Justice Sharswood,[7] "for the power of the directors to forfeit the stock. No doubt the power given must be strictly pursued, and if any restrictions or limitations therein

[1] McMillan v. Railway Co., 15 B. Mon. 218. See Buffalo, etc., R. Co. v. Gifford, 87 N. Y. 294. The sale of the property and franchises under a contract which is afterwards rescinded will not release the subscriber. Chattanooga, etc., R. Co. v. Warthen, 98 Ga. 599.

[2] Armstrong v. Karshner, 47 Ohio St. 276.

[3] Carter, etc., Co. v. Hazzard, 65 Minn. 432. Such a subscriber has the right to take part in the organization. People's, etc., Co. v. Balch, 8 Gray (Mass.) 303; Nickum v. Burckhardt, 30 Ore. 464, 60 Am. St. Rep. 822.

[4] Level Land Co. v. Hayward, 95 Wis. 109.

[5] Budd v. Multnomah, etc., R. Co., 15 Ore. 413, 3 Am. St. Rep. 169.

[6] In Lesseps v. Architects' Co., 4 La. An. 316, it was held that a forfeiture in pursuance of a by-law indorsed on the stock certificate was binding upon the stockholder, on the theory that it had been agreed to by all the members.

[7] Germantown, etc., R. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec. 546.

provided have been disregarded, the alleged act of forfeiture must be declared invalid. This is so for the special reason that it is one of those forfeitures against which, if regular, equity does not relieve. The right to forfeit shares in any joint stock undertaking must come from the law and can only be exercised in the manner provided by the law.[1] Hence, if the charter provides the method of procedure, it must be strictly followed.[2] "The company in enforcing the payment of calls by forfeiture must strictly pursue the mode pointed out in the charter and the general laws of the state. This is a rule of universal application to the subject of forfeiture, and one which the courts will rigidly enforce, and more especially where the forfeiture is one of the prescribed remedies given to the party against which equity does not relieve when fairly exercised."[3] Where the manner of giving notice is prescribed by the law under which calls are made, the directors "have no right to dispense with the mode and manner of notice thus prescribed, and where by positive law personal notice is required, a written notice through the mail is not a compliance with the statute."[4] In order to sustain a forfeiture, every condition precedent must be strictly and literally complied with.[5]

A declaration of forfeiture of shares in an incorporated joint stock company or partnership is void where the articles of association provide for the publication of notice in the newspapers of two designated cities for thirty days before declaring a forfeiture, and the notice is published in the papers of one city only.[6]

§ 388. **When forfeiture a cumulative remedy.**—Whether the right to forfeit shares for non-payment of assessments is a cumulative or exclusive remedy will depend upon the language

[1] Westcot v. Minnesota, etc., Co., 23 Mich. 145; In re Long Island Co., 19 Wend. (N. Y.) 37, 32 Am. Dec. 429.

[2] Allen v. American, etc., Assn., 55 Minn. 86.

[3] 1 Redfield Railways, p. 211, quoted in Morris v. Metalline, etc., Co., 164 Pa. St. 326, 27 L. R. A. 305.

[4] Hughes v. Antietam, etc., Co., 34 Md. 316; Macon, etc., Co. v. Vason, 57 Ga. 314.

[5] Morris v. Metalline, etc., Co., 164 Pa. St. 326, 27 L. R. A. 305; Mitchell v. Vermont, etc., Co., 8 Jones & Spen. 406; Johnson v. Lytle, etc., Agency, L. R. 5 Ch. Div. 687.

[6] Morris v. Metalline, etc., Co., 164 Pa. St. 326, 27 L. R. A. 305.

by which the power is granted. The general rule in the United States is that where a corporation has a statutory right to declare a forfeiture for non-payment of calls, it may exercise the option either to forfeit the shares, or bring an action to collect the amount of the call, but that it can not forfeit the shares and afterwards sue at law on the contract.[1] The exercise of the option to forfeit in such a case terminates the contractual relation between the corporation and the stockholder. The corporation can not even collect the amount of a prior assessment after a forfeiture, although a promissory note has been given for the amount.[2] An unsuccessful attempt to forfeit shares will not release the shareholder from personal liability as it has no effect upon the relation in which he stands to the corporation.[3] The question of the liability of the stockholder after forfeiture will depend upon the nature of the statutory remedy. If there is an absolute forfeiture, his liability ceases, but if the remedy provides for a sale of the shares, and an accounting, the amount received for the shares must be credited upon the liability, and the corporation may have its action to recover the unpaid balance. The sale in such case is in the nature of the foreclosure of a lien held by the corporation upon the shares.[4] In the states where it is held that an action can not be maintained on a subscription contract unless it contains an express promise to pay, such promise is necessary to support an action for a deficiency after a foreclosure and sale of the shares.[5]

§ 389. **Estoppel of subscriber.**—One who subscribes for shares can not avail himself of the irregularities in their issue if he has acquiesced or taken part in the transaction;[6] has

[1] Mandel v. Swan, etc., Co., 154 Ill. 177, 27 L. R. A. 313; Macon v. Vason, 57 Ga. 314; Lexington, etc., Co. v. Bridges, 7 B. Mon. (Ky.) 556, 46 Am. Dec. 528; Carson v. Mining Co., 5 Mich. 288; Connecticut, etc., R. Co. v. Bailey, 24 Vt. 465.

[2] Ashton v. Burbank, 2 Dill. (C. C.) 435.

[3] Instone v. Frankfort, etc., Co., 2 Bibb (Ky.) 576.

[4] Small v. Herkimer, etc., Co., 2 N. Y. 330; Rutland, etc., R. Co. v. Thrall, 35 Vt. 536.

[5] Mechanics', etc., Co. v. Hall, 121 Mass. 272; Katama, etc., Co. v. Jernegan, 126 Mass. 155.

[6] Clarke v. Thomas, 34 Ohio St. 96;

voluntarily paid an assessment thereon,[1] or has subscribed after their issue under circumstances from which it may be presumed that he has waived such irregularities.[2] But a subscriber who has done nothing upon which an estoppel may be based, may decline to receive shares improperly issued, and successfully defend a suit brought to recover on the subscription contract.[3] One who agrees to take shares in a corporation to be organized, who does not participate in the organization, is entitled to receive shares in a regularly and legally organized corporation. The right to membership in a particular corporation may be restricted by express provisions in its charter, but a stockholder may, under certain circumstances, be estopped to assert that he had not the necessary qualifications. Thus, where the defendants subscribed and paid for stock and accepted certificates therefor in a corporation which by its charter restricted the right to hold stock therein to persons of a certain nationality, and it appeared that the corporation accepted them as stockholders, and that, without objection on their part, they appeared as stockholders on the books of the corporation three years, during which time debts were contracted and the corporation became insolvent, it was held that they were estopped, as against creditors, to assert that they were not stockholders, because not, in fact, eligible to membership in the corporation.[4]

In an action to collect a subscription for the benefit of the corporation or its creditors, the stockholder can not defend on the ground that the corporation has not fully complied with the statutes regulating incorporation.[5] An estoppel to be

Kansas City, etc., Co. v. Harris, 51 Mo. 464.

[1] Delano v. Butler, 118 U. S. 634.

[2] Kansas City, etc., Co. v. Hunt, 57 Mo. 126.

[3] American Tube Works v. Boston, etc., Co., 139 Mass. 5; Reed v. Boston, etc., Co., 141 Mass. 454.

[4] Blien v. Rand (Minn.), 79 N. W. Rep. 606.

[5] Hickling v. Wilson, 104 Ill. 54; Hause v. Mannheimer, 67 Minn. 194, 69 N. W. Rep. 810; State Bank, etc., Co. v. Pierce, 92 Iowa 668; Wadesboro, etc., Co. v. Burns, 114 N. C. 353; Thompson v. Reno, etc., Bank, 19 Nev. 103; Hamilton v. Clarion, etc., R. Co., 144 Pa. St. 34; Swartwout v. Michigan, etc., R. Co., 24 Mich. 389. But see Kansas City, etc., Co. v. Hunt, 57 Mo. 126. §§ 368, 385.

availed of must be pleaded. Hence, if a corporation wishes to prevent defendants from controverting its corporate existence on the ground that they have dealt with it as a corporation, it must plead the estoppel.[1]

§ 389a. **The statute of limitations.**—There is some conflict in the authorities upon the question as to when the statute of limitations begins to run upon contracts of subscriptions to the capital stock of a corporation. The supreme court of the United States holds that the statute begins to run against an action against a stockholder in an insolvent corporation in the hands of a receiver to recover unpaid assessments on his stock when the court orders the assessment to be made.[2] The weight of authority establishes the rule that some adverse action on the part of the company or the representative of its creditors, such as the making of a call, is necessary before the statute begins to run.[3] An assessment is necessary, although the corporation is insolvent and in the hands of a receiver. A statute is considered as running from the time the call is due and payable. Another class of cases holds that an act of insolvency on the part of the corporation renders the obligation of the subscriber to pay absolute, and that the statute begins to run from that time without reference to a call.[4] Still others hold that if a call is not made within the time which bars actions upon contracts of like character, the company is presumed to have abandoned the contract.[5] The statute of the state by which the corporation is created governs.[6] The liability for an unpaid subscription must be distinguished from the additional liability for the debts of a corporation which is sometimes im-

[1] Nickum v. Burckhardt, 30 Ore. 464, 60 Am. St. Rep. 822.

[2] Glenn v. Marbury, 145 U. S. 499.

[3] Scovill v. Thayer, 105 U. S. 143; Thomas v. Reno Sav. Bank, 19 Nev. 171; Curry v. Woodward, 53 Ala. 371; Washington Sav. Bank v. Bank, 107 Mo. 133; Williams v. Taylor, 120 N. Y. 244.

[4] Glenn v. Dorsheimer, 23 Fed. Rep. 695, 24 Fed. Rep. 536; Franklin Sav. Bank v. Bridges (Pa.), 8 Atl. Rep. 611; Garesche v. Lewis, 93 Mo. 197.

[5] Pittsburgh, etc., R. Co. v. Byers, 32 Pa. St. 22; Morrison v. Mullin, 34 Pa. St. 12. If a subscription is conditional, the statute runs from the time of the performance of the condition. Cornell & Michler's App., 114 Pa. St. 153.

[6] Glenn v. Liggett, 135 U. S. 533.

posed by statute upon a stockholder for the benefit of creditors. It has been held that when the statute has run against the corporation it also bars an action by the creditors.[1] But the better rule is that, as against the creditors of the corporation, the statute begins to run from the date of their judgments against the corporation.[2]

[1] Stilphen v. Ware, 45 Cal. 110. See First Nat'l Bank v. Greene, 64 Iowa 445.

[2] Christensen v. Quintard, 36 Hun (N. Y.) 334; Christensen v. Colby, 43 Hun (N. Y.) 362.

CHAPTER 15.

THE RIGHTS OF MEMBERSHIP.

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§ 390. **Participation in the management.**—The members of a corporation have not ordinarily the right of direct participation in the management of the corporation. When the stockholders share in the election of directors, and of officers, if the election of officers is retained by the shareholders, they have no further right to a part in the management of the corporation.[1] Within the scope of their authority the directors act for the corporation. And in the exercise of the ordinary powers which are granted to the corporation their discretion can not be controlled by the stockholders.[2] But powers which are extraordinary, and which change the original contract of membership, such as the sale of the entire corporate property, or the acceptance of a material amendment to the charter, can not be exercised by the directors without express authority from the stockholders.[3]

§ 391. **General rights of stockholders.**—The rights of stockholders, as stated by a learned judge, are "to meet at stockholders' meetings, to participate in the profits of the business; and to require that the corporate property and funds shall not be diverted from their original purpose. If the company becomes insolvent, it is the right of the stockholders to have the property applied to the payment of its debts. I do not know of any other rights, except incidental ones subsidiary and auxiliary to these. Of course, the stockholder has ordinarily the right to a certificate for his stock, to transfer it on the company's books, and to inspect these books. For the invasion of these rights by the officers of the company, he may sue at law or in equity, according to the facts in the case."[4]

§ 392. **Rights in the corporate property.**—A shareholder in a corporation has no legal title to the property or profits in the corporation until a division is made or a dividend declared. He acquires no right or title to the accumulated gains from

[1] As to the right to vote, see § 471.

[2] Rathbone v. Parkersburg, etc., Co., 31 W. Va. 798, 8 S. E. Rep. 570.

[3] Marlborough, etc., Co. v. Smith, 2 Conn. 579. See ch. 18, on the management of corporations.

[4] Woods, J., in Forbes v. Memphis, etc., R. Co., 2 Woods C. C. 323.

the revenues of the corporation which entitles him to sue for his undivided share of the dividends. Until divided by the directors or trustees of the corporation, all of its property is held by the corporation itself, and no several right is possessed by the individual stockholder until a dividend is declared. The declaration of a dividend from a surplus or a division of profits is within those discretionary powers of the directors or trustees, which will not be controlled by the courts.[1] Under proper circumstances, however, the courts will recognize the fact that although the legal title to the property is in the corporation, the beneficial interest is in the stockholders. A court of equity will not permit the theory of the separate identity of the corporation to be used for the purpose of consummating a fraud or injuring the rights of the stockholders.[2]

§ 393. **Right to inspect records.**—A stockholder in a corporation has at common law the right to inspect and copy the books and records of the corporation at a convenient time and place[3] for proper purposes, in person or by his attorney-in-fact.[4] The right is very generally secured by statute, and in

[1] Parker v. Bethel Hotel Co., 96 Tenn. 252, 31 L. R. A. 706; Beveridge v. New York, etc., R. Co., 112 N. Y. 1, 2 L. R. A. 648; In re Kernochan, 104 N. Y. 618; Spooner v. Phillips, 62 Conn. 62, 16 L. R. A. 461; Gibbons v. Mahon, 136 U. S. 549. See § 400. In some cases it is held that a stockholder has an insurable interest in the property of the corporation. Seaman v. Insurance Co., 18 Fed. Rep. 250, although the contrary has been held. A stockholder has such an interest in a conveyance to or from a corporation as will disqualify him to take an acknowledgment as a notary. The authorities are collected in Kothe v. Krag-Reynolds Co. (Ind. App.), 50 N. E. Rep. 594. *Contra*, by statute, Minn. Gen. Laws, 1899, ch 62.

[2] Thus, in an appropriate case and in furtherance of the ends of justice, a debtor corporation and the owner of all its stock and assets will be treated as identical. Pott & Co. v. Schmucker, 84 Md. 535, 57 Am. St. Rep. 415. A stockholder is not a trustee for the corporation. Rogers v. Nashville, etc., R. Co., 91 Fed. Rep. 299.

[3] In re Steinway, 159 N.Y. 250, 53 N. E. Rep. 1103; Lewis v. Brainerd, 53 Vt. 519; Huylar v. Cragin, etc., Co., 40 N. J. Eq. 392; Commonwealth v. Phœnix, etc., Co., 105 Pa. St. 111, 23 Am. Law Reg. (N. S.) 388 and note; Bourdette v. New Orleans, etc., Co., 49 La. Ann. 1556.

[4] Foster v. White, 86 Ala. 467; State v. Bienville, etc., Works, 28 La. Ann. 204; Stone v. Kellogg, 165 Ill. 192; Deaderick v. Wilson, 8 Bax. (Tenn.) 108.

some cases the persons who refuse a stockholder the right to inspect the books are liable to a penalty which may be recovered without showing actual damages.[1] In Alabama it is provided that "the stockholders of all private corporations have the right of access to, of inspection and examination of, the books, records and papers of the corporation, at reasonable and proper times." Under this statute the stockholder "is not required to show any reason or occasion rendering an examination opportune and proper, or a definite or legitimate purpose. The custodian of the books and papers can not question or inquire into his motives and purposes. If he has reason to believe that they are improper or illegitimate, and refuses the inspection on this ground, he assumes the burden to prove them as such."[2] Where the statute provided that the stock books should "be open for the inspection of stockholders," it was held that mandamus would not lie when the demand was made by the stockholder's attorney.[3] But generally the right of the stockholder may be exercised in person, or through his agent or attorney.[4] The books must not be appropriated to an unreasonable extent, but access to them can not be denied simply because it would be inconvenient to grant it.

§ 394. **Conditions upon which inspection is permitted.**— Where there is no statute regulating the matter it is generally necessary that there should be some particular matter in dispute between the members or between the corporation and individuals in it, in which the applicant is interested, and in respect of which the examination of the books is necessary.[5] The stockholder must show a specific and proper purpose. As

[1] Kelsey v. Fermentation Co., 51 Hun (N. Y.) 636; Lewis v. Brainerd, 53 Vt. 510.

[2] Foster v. White, 86 Ala. 467. See also Winter v. Baldwin, 89 Ala. 483; State v. Bergenthal, 72 Wis. 314; State v. St. Louis, etc., R. Co., 29 Mo. App. 301.

[3] People v. U. S., etc., Co., 20 Abb. New Cas. 192; State v. St. Louis, etc., R. Co., 29 Mo. App. 301.

[4] Foster v. White, 86 Ala. 467, 6 So. Rep. 88; State v. Bienville, etc., Works, 28 La. Ann. 204; Phœnix, etc., Co. v. Commonwealth, 113 Pa. St. 563.

[5] Lyon v. American, etc., Co., 16 R. I. 472; Commonwealth v. Iron Co., 105 Pa. St. 111; Phœnix, etc., Co. v. Commonwealth, 113 Pa. St. 563; Commonwealth v. Pass. R. Co., 134 Pa. St. 237, 19 Atl. Rep. 629; State v. Einstein, 46 N. J. L. 479.

said by the Pennsylvania court, the right is not to be exercised to gratify curiosity or for speculative purposes, but in good faith, and for a specific honest purpose, and where there is a particular matter in dispute, involving and affecting seriously the rights of the stockholder.[1] The right of inspection does not exist merely for the purpose of gratifying an idle curiosity "at the caprice of the curious and suspicious."[2] The fact of general dissatisfaction with the management of the enterprise, based upon a vague belief that it is being improperly conducted,[3] or that the stockholder wishes to discover grounds on which to base charges against the corporate body,[4] or to use the information for speculative or fraudulent ends,[5] or to prove a plea of justification in an action against the stockholders for libel in imputing insolvency to the company, is not sufficient to justify a demand for inspection.[6] But an inspection may be granted to a stockholder on a prima facie showing of fraud to secure information for a bill to obtain relief against the fraud.[7]

As a general rule mere suspicion that there has been mismanagement is not sufficient to entitle a stockholder to a writ of mandamus, although it has been held on good grounds that a stockholder is entitled to examine the records in order to learn whether the affairs of the corporation are being properly conducted by the directors. "To say that they have the right, but that it can be enforced only when they have ascertained in some way without the books that their affairs have been mismanaged, or that their interests are in danger, is practically to deny the right in the majority of cases. Oftentimes frauds

[1] Phœnix, etc., Co. v. Commonwealth, 113 Pa. St. 563.

[2] People v. Walker, 9 Mich. 328.

[3] Lyon v. American, etc., Co., 16 R. I. 472.

[4] Commonwealth v. Phœnix, etc., Co., 105 Pa. St. 111.

[5] In re Sage, 70 N. Y. 220; Commonwealth v. Iron Co., 105 Pa. St. 111.

[6] M. S. O. Co. v. Hawkins, 4 Hurl. & N. 146.

[7] Phœnix, etc., Co. v. Commonwealth, 113 Pa. St. 563. As to right to order the corporate books brought within the state for inspection, see Mitchell v. Rubber Co. (N. J. Ch.), 24 Atl. Rep. 407; Swift v. Richardson, 7 Houst. (Del.) 338.

are discoverable only by examination of the books by an expert accountant. The books are not the private property of the directors or managers, but are the records of their transactions as trustees for the stockholders.[1]

§ 395. **The demand.**—If the stockholder desires to examine the records of the corporation, it is his duty to make proper demand upon the officers in charge of the same, and to state the reason for which he wishes to make the examination, and the specific and particular books and records he desires to inspect. A demand of the privilege of inspecting all the books and records of a corporation is too broad and indefinite, and need not be complied with.[2]

§ 396. **Remedy for wrongful refusal to permit inspection.**—If a stockholder is wrongfully refused the privilege of inspecting the books and records of the corporation upon a proper demand made at the proper time, he may maintain an action for damages against the corporation, or petition for a writ of mandamus to compel the custodian to permit the inspection.[3] The

[1] Huylar v. Cragin Cattle Co., 40 N. J. Eq. 392, 2 Atl. Rep. 274.

[2] See Foster v. White, 86 Ala. 467.

[3] The right of a corporator, who has an interest, in common with the other corporators, to inspect the books and papers of the corporation, for a proper purpose and under reasonable circumstances, was recognized by the courts of king's bench and chancery from an early day, and enforced by motion or mandamus, but always with caution, so as to prevent abuse. Rex v. Fraternity of Hostmen, 2 Strange 1223, and note; Gery v. Hopkins, 7 Mod. 129, case 175; Richards v. Pattinson, Barnes, Notes Cas. 235; Young v. Lynch, 1 W. Bl. 27; Rex v. Shelley, 3 Term R. 141; Rex v. Babb, Id. 579, 580; Rex v. Merchant, etc., Co., 2 Barn. & Adol. 115; In re Burton, L. J. 31 Q. B. 62; In re West Devon Great Consols Mine, L. R. 27 Ch. Div. 106. Lord Kenyon, in rendering judgment in Rex v. Babb, assumed "that in certain cases the members of a corporation may be permitted to inspect all papers relating to the corporation." In Gery v. Hopkins, the court, on granting the order to produce, said: "There is great reason for it, for they are books of a public company and kept for public transactions, in which the public are concerned, and the books are the title of buyers of stock, by act of parliament." In Rex v. Fraternity of Hostmen, the reporter states that the court said: "Every member of the corporation had, as such, a right to look into the books for any matter that concerned himself, though it was in dispute with others." In re Steinway (N. Y.), 53 N. E. Rep. 1103; Com. v. Phœnix, etc., Co., 105 Pa. St. 111; Lyon v. American, etc., Co., 86 R. I. 472, 17

granting of the writ, however, is not imperative, but rests within the sound discretion of the court.[1] The corporation is not a necessary party, as the writ may issue against the officer having the custody of the books and records in question.[2] It is also held that a stockholder who is wrongfully denied the right to inspect the corporate records may recover the damages he sustains thereby from the corporation,[3] or recover a penalty which is provided by statute.[4]

§ 397. **Preference in subscription for new shares.**—When a corporation increases its capital stock, the members, at the time of the vote to issue the new stock, are entitled to the privilege of subscribing for the new stock in proportion to their respective shares of the old.[5] The right is now commonly secured by statute,[6] and passes to the transferee of the original stock. The option may be sold.[7]

Each of the stockholders in a corporation formed by the union of two corporations under an agreement that the capital stock shall be divided into four different classes, with provisions for the payment of different dividends on each class, on an increase of the capital stock is entitled to purchase in proportion to the amount of stock held by him.[8]

Atl. Rep. 61; Foster v. White, 86 Ala. 467, 6 So. Rep. 88; Stone v. Kellogg, 62 Ill. App. 444; Huylar v. Cattle Co., 40 N. J. Eq. 392, 2 Atl. Rep. 274; Stettauer v. New York, etc., Co., 42 N. J. Eq. 46; Cockburn v. Union Bank, 13 La. An. 289.

[1] Rex v. W. & B. C., etc., Co., 3 Ad. & El. 477; People v. Walker, 9 Mich. 328; Foster v. White, 86 Ala. 467; People v. Paton, 20 Abb. N. Cas. 195; In re Sage, 70 N. Y. 221.

[2] State v. Bergenthal, 72 Wis. 314, 39 N. W. Rep. 566; Swift v. Richardson, 7 Houst. (Del.) 338; Foster v. White, 86 Ala. 467.

[3] Legendre & Co. v. Association, 45 La. An. 669.

[4] Lewis v. Brainerd, 53 Vt. 519.

[5] Gray v. Portland Bank, 3 Mass. 364; Jones v. Morrison, 31 Minn. 140; Dousman v. Wisconsin, etc., Co., 40 Wis. 418; Humboldt, etc., Assn. v. Stevens (Neb.), 52 N. W. Rep. 568; Ohio, etc., Co. v. Nunnemacher, 15 Ind. 294; Mason v. Davol Mills, 132 Mass. 76; Eidman v. Bowman, 58 Ill. 444; Jones v. Concord, etc., R. Co. (N. H.), 38 Atl. Rep. 120.

[6] Cunningham's Appeal, 108 Pa. St. 546. The stockholders can not be charged a bonus on the stock to which they are given a right to subscribe.

[7] Baltimore, etc., R. Co. v. Hambleton (Md., 1893), 26 Atl. Rep. 279; Biddle's Appeal, 99 Pa. St. 278.

[8] Jones v. Concord, etc., R. Co., 67 N. H. 119, 38 Atl. Rep. 120.

This rule, however, does not apply where the stock is issued for the purchase of property which will become a part of the common property of the corporation.[1]

I. Dividends.

§ 398. **Nature of dividends.**—Dividends are the moneys paid by corporations to the shareholders out of the profits earned in the business.[2] They are said to be the corporate funds derived from the business and earnings of the corporation, appropriated by a corporate act to the use of and to be divided among the stockholders.[3] A distinction is thus made between dividends and profits. Profits belong to the corporation and not to the stockholder until after they have been declared by some proper corporate act. After a dividend is declared, the amount apportioned to the individual stockholder becomes a debt of the corporation and the stockholder may sue the corporation to recover it in the same manner as any other debt. After a dividend is declared, it becomes the property of the individual stockholder, but an accumulated surplus in existence at the time of the insolvency of a corporation goes to the corporate creditors and not to the stockholders.[4] In a case where certain stockholders of an insolvent insurance company claimed the surplus funds of the company beyond the capital stock, Chancellor Walworth said:[5] "The claim is founded on the erroneous supposition that it is the duty of the directors of an insurance company to divide all its surplus funds beyond its capital stock periodically among the stockholders; leaving such capital stock alone as the fund to which the creditors of the company who become such by the loss of property insured are to look for remuneration, but * * * the capital stock of an incorporated insurance company is not the primary or natural fund for the payment of losses which

[1] Meredith v. New Jersey, etc., Co., 55 N. J. Eq. 211.

[2] Hyatt v. Alton, 56 N. H. 553.

[3] Hagar v. Union Nat'l Bank, 63 Me. 509, and cases therein cited.

[4] Beers v. Bridgeport Spring Co., 42 Conn. 17; Lockhart v. Van Alstyne, 31 Mich. 76; Beveridge v. Railway Co., 112 N. Y. 1.

[5] Scott v. Eagle, etc., Co., 7 Paige N. Y. 198.

may happen by the destruction of the property insured. The charter of the company contemplates the interest upon the capital stock, and the premiums received for insurance, as the ordinary fund out of which losses are to be paid. And the surplus of that fund, after paying such losses, is surplus profits within the meaning of the charter; which surplus profits alone are to be divided, from time to time, among the stockholders."

§ 399. **Control of directors over dividends.**—The stockholders have no absolute right to have a dividend declared, as the matter rests ordinarily in the discretion of the directors. So long as this discretion is honestly exercised, it will not be controlled by the court.[1] "The directors of a corporation, and they alone, have the power to declare a dividend of the earnings of the corporation and to determine the amount."[2] The discretion must not be abused,[3] but it is necessary to make a very strong case before the courts will interfere.[4] The supreme court of the United States recently said:[5] "Money earned by a corporation remains the property of the corporation and does not become the property of the stockholders unless and until it is distributed among them by the corporation. The corporation may treat it and deal with it either as profits of its business or as an addition to its capital. Acting in good faith and for the best interests of all concerned, the corporation may distribute its earnings at once to the stockholders as income; or it may reserve part of the earnings of a prosperous year to make up a possible lack of profit in future

[1] Gibbons v. Mahon, 136 U. S. 549; Kaufman v. Woolen Mills Co. (Va.), 25 S. E. Rep. 1003; Fourgeray v. Cord, 50 N. J. Eq. 185; Pratt v. Pratt, etc., Co., 33 Conn. 446; Beers v. Bridgeport, etc., Co., 42 Conn. 17. The directors may make any distribution of profits which they deem judicious, when they are not restrained by the charter or by contract. Park v. Grant, etc., Works, 40 N. J. Eq. 114.

[2] Hunter v. Roberts, etc., Co., 83 Mich. 63; Grant v. Ross (Ky.), 37 S. W. Rep. 263.

[3] Laurel Springs, etc., Co. v. Fougeray, 50 N. J. Eq. 756; Miner v. Bell Isle Ice Co., 93 Mich. 97.

[4] New York, etc., R. Co. v. Nickals, 119 U. S. 296; Park v. Grant, etc., Works, 40 N. J. Eq. 114; McNab v. McNab, etc., Co., 62 Hun (N. Y.) 18; Zellerbach v. Allenberg, 99 Cal. 57.

[5] Gibbons v. Mahon, 136 U. S. 549.

years; or it may retain portions of its earnings and allow them to accumulate and then invest them in its own plant, so as to secure and increase the permanent value of its property. Which of these courses is to be pursued is to be determined by the directors with due regard to the conditions of the company's property and affairs as a whole; and, unless in case of fraud or bad faith on their part, their discretion in this respect can not be controlled by the courts, even at the suit of owners of preferred stock, entitled by express agreement with the corporation to dividends at a certain yearly rate in preference to the payment of any dividend on the common stock but dependent on the profits of each particular year as declared by the board of directors. By becoming a member of a corporation, a stockholder impliedly contracts with the corporation that his interests shall be subject to the direction and control of the corporate authorities of the corporation for the purpose of accomplishing the ends for which the corporation was created.[1] "The directors of such corporations have opportunities not ordinarily possessed by others of knowing the resources and conditions of the property under their control; and are in a better position than stockholders to determine whether, in view of the duties which the corporation owes to the public and of all liabilities, it will be prudent in any particular year to declare a dividend upon the stock. While their authority in respect of these matters may, of course, be controlled or modified by the company's charter, and while the power of the courts may be invoked for the protection of the stockholders against bad faith upon the part of the directors, we should hesitate to assume that either the legislature or the parties intended to deprive a corporation, by its managers, of the power to protect the interests of all, including the public, by using earnings when necessary, or when in good faith believed to be necessary, for the preservation or improvement of the property intrusted to its control."[2] Hence mandamus will not lie

[1] Clearwater v. Meredith, 1 Wallace (U. S.) 25.

[2] New York, etc., R. Co. v. Nickals, 119 U. S. 296.

to compel the directors to declare a dividend unless there is a manifest abuse of discretion or a lack of good faith.[1]

§ 400. **Discretion of directors.**—The free exercise of discretion by the directors in reference to the declaration of dividends can not be interfered with by contracts of promoters, unless such contracts were ratified by the corporation after its organization.[2] As above stated, the rule is that the directors are the sole judges of the propriety of declaring a dividend; but they are not allowed to act illegally, wantonly or oppressively. When the right to a dividend is clear and there are funds from which it can properly be made, a court of equity will compel the company to declare it.[3] The mere fact that the income of the corporation exceeds its liabilities for the year does not entitle the stockholder to have a dividend declared.[4] As the directors "are bound to exercise a proper discretion in making a dividend of surplus profits, if they abuse that power * * * they may, in case of any extraordinary loss, * * * make themselves personally liable to the creditors of the company. On the other hand, should they, without reasonable cause, refuse to divide what is actually surplus profits, the stockholders are not without remedy if they apply to the proper tribunal, before the corporation becomes insolvent."[5]

§ 401. **Protection of corporate property.**—It is the duty of the directors to set aside a fund sufficient to make good the depreciation of the property of the corporation.[6] The fund available for dividends is ascertained by taking into account the cost of repairs and a reasonable allowance for depreciation for wear and tear or constant use, giving credit for all actual improvements.[7] But this principle does not apply when the

[1] March v. Eastern R. Co., 43 N. H. 515; King v. Bank, etc., 2 Barn. & Ald. 620.

[2] Coyote, etc., Co. v. Ruble, 8 Ore. 284.

[3] Richardson v. Vermont, etc., R. Co., 44 Vt. 613.

[4] Belfast, etc., Co. v. Belfast, 77 Maine 445; Fougerary v. Cord, 50 N. J. Eq. 185.

[5] Scott v. Eagle, etc., Co., 7 Paige (N. Y.) 198.

[6] Davidson v. Gillies, L. R. 16 Ch. Div. 347.

[7] Whittaker v. Amwell Nat'l Bank, 52 N. J. Eq. 400.

corporation is operated for the purpose of using up certain property, such as a mine. Under such circumstances the transaction of business necessarily reduces the value of the property which gives value to the stock. Hence, a mining corporation may distribute as dividends the net profits of its operations without reference to the depreciation of its property caused by removing its ore.[1] A mining company which has paid interest out of capital on debentures during the time when the mine was closed by reason of an accident is not bound to apply profits in replacing the amount so paid before declaring a dividend to stockholders.[2] In estimating the profits for a year for the purposes of a dividend, it is not necessary to take into account the decrease in the value of the assets and the impairment of the capital stock prior to that year.[3] When the capital of a corporation is reduced under authority of law, the corporation must, before it distributes the fund thus created among the stockholders, retain enough to make the reduced capital of the actual value of the face of the stock.[4]

§ 402. **When dividends may be legally declared.**—Ordinarily a dividend can only be paid out of net profits,[5] although, if there are no creditors and no dissenting stockholders, there is no objection to the corporation distributing its capital among its stockholders in the form of dividends.[6] Generally, however, if there are no accumulated profits, a dividend which necessarily results in a partial distribution of the assets to the detriment of creditors and stockholders is illegal.

§ 403. **What are profits.**—The "profits," out of which dividends alone can properly be declared, means simply what remains after defraying every expense.[7] It generally means the

[1] Excelsior, etc., Co. v. Pierce, 90 Cal. 131, 27 Pac. Rep. 44.

[2] Bosanquet v. St. John, etc., Co. (Ch.), 77 Law T. Rep. 206.

[3] Bolton v. Natal, etc., Co., 65 Law T. Rep. (N. S.) 786.

[4] Seely v. Bank, 78 N. Y. 608; Strong v. Railway Co., 93 N. Y. 426.

[5] Main v. Mills, 6 Biss. (C. C.) 98.

[6] People v. Barker, 141 N. Y. 251. Under statutory authority, see H. L. 75 Law T. Rep. 3.

[7] Mobile, etc., R. Co. v. Tennessee, 153 U. S. 486. For definitions of

gain which comes or is received from any kind of an investment where both receipts and expenses are taken into account. Thus, profits for the year means the surplus receipts after paying expenses and restoring the capital to the condition it was in on the first day of the year. The net earnings of a railroad are the gross receipts, less the operating expenses of the road to earn such receipts, and among the expenses should be included the interest on its debt. The net profits of an insurance company are the difference between the amount of the losses and the sum of the premiums earned and received from insurance and the interest on the capital. The capital stock of

profits, see St. John v. Erie R. Co., 10 Blatch. (U. S.) 271; Warren v. King, 108 U. S. 389; Eyster v. Centennial Board, 94 U. S. 500; Phillips v. Eastern R. Co., 138 Mass. 122; Richardson v. Buhl, 77 Mich. 632; Hubbard v. Weare, 79 Iowa 678. In People v. San Francisco Sav. Union, 72 Cal. 199, the court said: "The word profits signifies an excess of the value of returns over the value of advances, the excess of receipts over expenditures; that is, net earnings." Connolly v. Davidson, 15 Minn. 519, Gil. 428. The receipts of a business deducting current expenses. It is equivalent to net receipts. Eyster v Centennial Board, 94 U. S. 500. In commerce it means the advance of goods sold beyond the cost of purchase. In distinction from the wages of labor, it is well understood to imply the net returns to the capital or stock employed after deducting all the expenses, including not only the wages of those employed by the capitalists but the wages of the capitalist himself for superintending the employment of his capital stock. Smith, Wealth of Nations, book 1, ch. 6; Mill, Political Economy, ch. 15. The rents and profits of an estate. The income or net income are all equivalent expressions. Andrews v. Boyd, 5 Maine 200; Earl v. Rowe, 35 Maine 414. Profits are divided by writers on political economy into gross and net, the former being the difference between the value of advances and the value of returns, and the latter so much of this difference as arises exclusively from the capital employed. In People v. Board of Supervisors, 4 Hill (N. Y.) 20, Bronson, J., said: "It is undoubtedly true that profits and income are sometimes used as synonymous terms; but, strictly speaking, income means that which comes in or is received from any business or investment of capital without reference to the outgoing expenditure; while profits generally mean the gain which is made upon any business or investment when both receipts and payments are taken into account. Income, when applied to the affairs of individuals, expresses the same idea that revenue does when applied to the affairs of a state or nation. In St. John v. Erie R. Co., 10 Blatch. 271, it was said: 'Net earnings are properly the gross receipts, less the expense of operating the road or other business of the corporation. Interest on debts is paid out of what thus remains; that is, out of the net earnings. The remainder is the profit of the shareholders.'"

such a company is not the primary fund from which losses are to be paid. Unearned premiums on insurance, which is still subject to the risk, are not surplus profits out of which dividends can be declared. The unearned premiums received by the company upon which the risks are still running, and which may therefore all be wanted to pay losses, are not surplus profits which the directors are authorized by the charter to distribute among the stockholders. The capital stock of the company is a special fund provided by its charter to secure the assured against great and extraordinary losses which the primary funds may be found insufficient to meet. And if it becomes necessary at any time to break in on this special fund to pay extraordinary losses, it must be made good from the future profits of the company before any further dividends of those profits can be made.[1] A mutual insurance company, when not restricted by statute or by-law, may pay a dividend to the members under certain circumstances, although the effect is to reduce the assets of the company provided for the payment of losses.[2] Money paid on stock as a part payment, which is afterwards forfeited, is not to be considered as profits.[3] Money paid to compensate a corporation for land taken under the power of eminent domain becomes part of the capital and can not be distributed as profits.[4] Generally, in order to determine whether there are any profits, it is necessary to deduct from the capital the amount of the capital stock and the expenses and losses sustained.[5] Borrowed money is, of course, not profits,[6] although it has been held that under a statute which restricted the payment of dividends to surplus profits, where earnings which might properly have been used for

[1] Lexington, etc., Co. v. Page, 17 B. Mon. (Ky.) 412; Scott v. Fire Ins. Co., 7 Paige Ch. (N. Y.) 198.

[2] McKean v. Biddle, 181 Pa. St. 361.

[3] Gratz v. Redd, 4 B. Mon. 178-197.

[4] Heard v. Eldredge, 109 Mass. 258, 12 Am. Rep. 687.

[5] "The words net profits define themselves. They mean what shall remain as the clear gains of any business venture, after deducting the capital invested in the business, the expenses incurred in its conduct, and the losses sustained in its prosecution." Park v. Grant, etc., Works, 40 N. J. Eq. 114; Main v. Mills, 6 Bissell 98. See Miller v. Bradish, 69 Iowa 278; Hubbard v. Weare, 79 Iowa 678.

[6] Davis v. Mining Co., 2 Utah 74.

dividends were used for improving the property of the corporation, it could borrow money to pay the dividends.[1] In this case it used the legitimate profits for the purpose for which it could properly have borrowed the money. An agreement to pay a fixed dividend on stock is valid so long as there are profits out of which to pay it,[2] but it can not be enforced where there are no profits and its payment would result in a distribution of the capital.[3] A bank can not declare dividends out of interest not yet received. "Money earned as interest, however well secured or certain to be eventually paid, can not in fact be distributed as dividends to stockholders and does not constitute surplus profits."[4] They do not become such until actually paid.

§ 404. **Right to dividends declared.**—As already stated, a stockholder has no title to profits accumulated by a corporation, so long as a dividend is not actually declared out of such surplus.[5] Until this is done the title to the fund remains in the corporation. As soon, however, as the dividend is declared, the title passes to the shareholders as individuals and the amount thus placed to the credit of the shareholder becomes a debt due to him from the corporation. Thereafter the relations between the corporation and the stockholder as to the dividend is that of debtor and creditor. The dividend is the property of the stockholder and can not be taken by the creditors of the corporation in the event of the insolvency of the corporation.[6] In case of insolvency, no specific dividend fund having been set aside, the shareholder must come in and share with the other creditors.[7] After a dividend is declared a corporation has no power to revoke its action and refuse to pay the

[1] Excelsior, etc., Co. v. Pearce, 90 Cal. 131.

[2] McLaughlin v. Railroad Co., 8 Mich. 99.

[3] Painesville R. Co. v. King, 17 Ohio St. 534.

[4] People v. San Francisco, etc., Union, 72 Cal. 199; Miller v. Bradish, 69 Iowa 278.

[5] Kaufman v. Woolen, etc., Co. (Va.), 25 S. E. Rep. 1003.

[6] LeRoy v. Insurance Co., 2 Edw. Ch. N. Y. 657; Van Dyck v. McQuade, 86 N.Y. 38; Peckham v. Van Wagenen, 83 N. Y. 40. Dividends declared can not be taxed as the property of a corporation. Pollard v. First Nat'l Bank, 47 Kan. 406.

[7] Curry v. Woodward, 44 Ala. 305.

dividend, in order to carry the account to a surplus fund.[1] But it was held in Massachusetts that a vote declaring a dividend could be rescinded at any time before the fact that a dividend had been declared was made known to the public or communicated to the stockholders.[2]

§ 405. **To whom dividends belong.**—The general rule is that dividends belong to the owner of the stock at the time when they are declared, without reference to the time when earned or payable. The declaration of a dividend is, in legal contemplation, the separation of the amount thereof from the assets of the corporation, and the corporation thereafter holds the amount as the trustee of the party who was a stockholder at the time it was declared.[3] The dividends are treated as though earned at the time they are declared, and hence the vendee of the shares is entitled to all dividends declared after the transfer.[4] The ownership of dividends may, of course, be made

[1] Beers v. Bridgeport Spring Co., 42 Conn. 17; King v. R. Co., 29 N. J. Law 82; In re Le Blanc, 75 N. Y. 598; Ford v. Thread Co., 158 Mass. 84, 32 N. E. Rep. 1036; Wheeler v. Sleigh Co., 39 Fed. Rep. 347. The purchaser of stock upon which, before its delivery, a dividend has been declared has no right to refuse to pay for the stock until the seller gives him an order on the corporation for the payment of the dividend. If he is entitled to the payment of the dividend such an order is unnecessary and he has no right to exact it. By insisting upon the order, and refusing to make payment without it, he rescinds the contract and loses both the stock and the dividend. If, after the contract is made for the sale of the shares of stock, but before the time appointed for paying therefor, a dividend is declared, the purchaser is entitled thereto on complying with his contract to purchase. Phinizy v. Murray, 83 Ga. 747, 20 Am. St. Rep. 342.

[2] Ford v. Thread Co., 158 Mass. 84. See In re Le Blanc, 75 N. Y. 598.

[3] Hopper v. Sage, 112 N. Y. 530, 8 Am. St. Rep. 771; Boardman v. Lake Shore, etc., R. Co., 84 N. Y. 157; In re Karnochan, 104 N. Y. 618; Goodwin v. Hardy, 57 Maine 143, 99 Am. Dec. 758, and note.

[4] Jermain v. Lake Shore, etc., R. Co., 91 N. Y. 483; Hill v. The Newichawanick Company, 71 N. Y. 593; Ryan v. Leavenworth, etc., R. Co., 21 Kan. 365; Gemmell v. Davis & Co., 75 Md. 546; Cook v. Munroe, 45 Neb. 349. A transfer passes all dividends declared subsequent to the transfer, although earned before. Kane v. Bloodgood, 7 Johnson's Ch. 90; Currie v. White, 45 N. Y. 822. No matter when payable. Wheeler v. Sleigh Co., 39 Fed. Rep. 347; Bright v. Lord, 51 Ind. 272; Hopper v. Sage, 112 N. Y. 530. *Contra*, Burrows v. North Carolina R. Co., 67 N. C. 376.

the subject of contract between the vendor and the purchaser of shares.[1] The corporation is entitled to rely upon its register, and, if it has no notice of the rights of any other person, it will be protected if it pay its dividends to the person in whose name the shares stand on its books.[2] After notice of a transfer, however, it must pay subsequent dividends to the transferee, although the shares have not been transferred on its books.[3] Corporations commonly provide that their transfer books shall be closed a certain number of days before a dividend is declared. Such regulations, in the absence of restrictive statutes, are valid.[4] Membership in a corporation does not depend upon the possession of a certificate of stock, and therefore a person who is actually a stockholder is entitled to a dividend, duly declared, although he may never have received a certificate.[5]

§ 406. **Collection of dividends.**—A dividend already declared may be recovered in an action at law by the stockholder against a corporation.[6] A suit to enforce the declaration of a dividend must be in equity. The action to recover a declared dividend should be against the corporation and not the corporate officers.[7] It can not be against an individual stockholder who has received a dividend which it is claimed belongs to the plaintiff.[8] Mandamus is not the proper remedy to com-

[1] Union, etc., Co. v. American, etc., Co., 11 R. I. 569, 13 R. I. 673; Kaufman v. Woolen Mills Co., 93 Va. 673.

[2] Brisbane v. Delaware, etc., R. Co., 94 N. Y. 204; Donnally v. Hearndon, 41 W. Va. 519; Bank of Com. Appeal, 73 Pa. St. 59.

[3] Robinson v. New Berne Nat'l Bank, 95 N. Y. 637.

[4] Jones v. Terre Haute, etc., R. Co., 57 N. Y. 196; Robinson v. New Berne Nat'l Bank, 95 N. Y. 637.

[5] Ellis v. Essex Bridge, 19 Mass. 243. As to the right of corporation to pay dividends to husband of the owner of the shares, see Graham v. First Nat'l Bank, 84 N. Y. 393; Dow v. Gould, etc., Co., 31 Cal. 629.

[6] Winchester, etc., Co. v. Wickliffe, 100 Ky. 531, 66 Am. St. Rep. 356; Jackson v. Newark, etc., Co., 31 N. J. Law 277; Westchester, etc., R. Co. v. Jackson, 77 Pa. St. 321; Hall v. Rose Hill, etc., Co., 70 Ill. 673; Southwestern, etc., R. Co. v. Martin, 57 Ark. 355; Hill v. Atoka, etc., Co., 21 S. W. Rep. 508.

[7] French v. Fuller, 40 Mass. 108; Smith v. Poor, 40 Maine 415.

[8] Peckham v. Van Wagenen, 83 N. Y. 40.

pel payment of a dividend.[1] Before suit is brought a demand is necessary,[2] although it has been held that the bringing of a suit is a sufficient demand.[3] A dividend draws no interest until a demand for its payment has been made and refused.[4] It is generally held that the statute of limitations begins to run from the time of the demand,[5] although some courts hold that it begins to run from the time when the right to make the demand accrues.[6] In an action brought to enforce the payment of dividends which have been declared the corporation can not raise the question of the validity of the dividend.[7] If a stockholder is unlawfully excluded from participation in a dividend, his remedy is against the corporation.[8] Where a corporation declares a dividend on all its stock except the shares named in a certain certificate, the exception is void and the owner of the certificate may sue the corporation to recover the dividend.[9] Dividends are payable within a reasonable time after they are declared.[10]

§ 407. **How payable—No discrimination.**—When not restricted by charter the manner of paying a dividend is under

[1] Van Norman v. Central Car, etc., Co., 41 Mich. 166.

[2] Winchester, etc., Co. v. Wickliffe, 100 Ky. 531, 66 Am. St. Rep. 356; Hagar v. Union Nat'l Bank, 63 Maine 509; King v. Paterson, etc., R. Co., 29 N. J. Law 504; Ford v. Easthampton, etc., Co., 158 Mass. 84, 35 Am. St. Rep. 462; Landis v. Saxton, 105 Mo. 486, 24 Am. St. Rep. 403; Fee v. Fee, 10 Ohio 469, 36 Am. Dec. 103. See Goodwin v. Hardy, 99 Am. Dec. 758, and note.

[3] Robinson v. Newburne Nat'l Bank, 95 N. Y. 637.

[4] Philadelphia, etc., R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128; Thompson Corps., § 223; Boardman, v. Lake Shore, etc., R. Co., 84 N. Y. 157; Bank of Louisville v. Gray, 84 Ky. 565. Interest does not run on a dividend which has been attached prior to the time of the demand for its payment. Mustard v. Union Nat'l Bank, 86 Maine 177.

[5] Bank of Louisville v. Gray, 84 Ky. 565.

[6] Winchester, etc., Co. v. Wickliffe, 100 Ky. 531, 66 Am. St. Rep. 356.

[7] Stoddard v. Foundry Co., 34 Conn. 542.

[8] Peckham v. Van Wagenen, 83 N. Y. 40; Jones v. Railway Co., 57 N. Y. 196.

[9] Hill v. Atoka, etc., Co. (Mo.), 21 S. W. Rep. 508. Where the corporation refuses to transfer the certificate to the one entitled to it, he may sue the corporation and recover the dividend without first bringing an action to compel the transfer. See Hughes v. Vermont, etc., Co., 72 N. Y. 207.

[10] Beers v. Bridgeport, etc., Co., 42 Conn. 17.

the control of the directors and may be in cash, property or in dividend stock. In a New York case it was said:[1] "There is no statute which requires dividends in telegraph companies or in companies generally to be made in cash. Whether they shall be made in cash or property must always rest in the discretion of the directors. There is no rule of law or reason founded upon public policy which condemns a property dividend. The directors could convert the property into cash for a dividend and divide that. So the stockholders can take the property divided to them and sell it and thus realize the cash. Within the domain of law it can make no material difference which course is chosen. If, however, a dividend is made payable in cash, or payable generally, the corporation becomes a debtor and must discharge such debts as it is bound to discharge all its other debts, in lawful currency. It is true that a stockholder can not be compelled to take property divided to him; he can not be compelled to take cash dividends. In case of his refusal to take the cash dividends, the corporation may retain it until he shall demand it. In case he shall refuse to take a property dividend, the corporation may retain it and hold it in trust for him, or possibly sell it for his benefit." But there can be no discrimination between stockholders,[2] and this applies to stock which has not been paid in full.[3] Thus, where stock is issued to contractors before they have completed their work, they are entitled to the dividends thereafter declared.[4] After paying a part of the dividend, a corporation can not refuse to pay the other stockholders because the money has been invested in improvements.[5]

§ 408. **Rights of a pledgee of stock to dividends.**—A pledgee whose name appears upon the books of the corporation or

[1] Williams v. Western U. Tel. Co., 93 N. Y. 162.

[2] State v. Baltimore, etc., R. Co., 6 Gill. (Md.) 363; Luling v. Atlantic, etc., Co., 45 Barbour (N. Y.) 510; Hale v. Republican, etc., 8 Kan. 466.

[3] Oak Bank, etc., Co. v. Crum, L. Rep. 8 App. Cas. 65. In Baltimore, etc., R. Co. v. Hambleton, 77 Md. 341, a distinction is made between original and increased stock.

[4] Central, etc., R. Co. v. Papot, 59 Ga. 342, 67 Ga. 675.

[5] Beers v. Bridgeport, etc., Co., 42 Conn. 17.

whose rights are otherwise known to the corporation is as between himself and the corporation entitled to dividends declared, and the corporation is liable to him if it pays the dividends to the pledgor.[1] As between the vendor and the vendee and the pledgor and pledgee of shares, a transfer on the books of the corporation is not necessary to perfect an equitable title in the vendee. Hence, dividends declared during the continuance of a pledge belong to the pledgee, although the shares have not been transferred to him on the books of the corporation. But if the transfer is not registered and the corporation in good faith pays the dividends to the pledgor, it will be protected.[2] The knowledge of the president, secretary and treasurer of the corporation is the knowledge of the corporation.

§ 409. **Unlawful payment of dividends—Liability of officers.**—In the absence of a statutory provision the directors of a corporation, when they act in good faith, are not liable to the shareholders or creditors of the corporation for damages resulting from the payment of illegal dividends.[3] An absolute liability is sometimes imposed by statute.[4] The directors are in all cases liable if they act fraudulently or are guilty of gross negligence.[5] It would seem upon well settled general principles that "if dividends were made under a misconception on the part of the directors of what constituted profits,

[1] Boyd v. Worsted Mills, 149 Pa. St. 363, 24 Atl. Rep. 287; Gemmell v. Davis & Co., 75 Md. 546; Central, etc., Co. v. Wilder, 32 Neb. 454, 49 N. W. Rep. 369. The pledgee is as a general rule entitled to the dividends unless the right is reserved to the pledgor. "The dividends follow the stock into the hands of the person who is the legal holder of the stock. While the general property in the stock remains in the pledgor, the pledgee has such a title therein as will authorize and require him to collect the dividends." Guaranty Co. v. East, etc., T. Co., 96 Ga. 511; Armour & Co. v. East, etc., T. Co., 98 Ga. 458, 25 S. E. Rep. 504.

[2] Gemmell v. Davis & Co., 75 Md. 547; Hill v. Mewichawanick Co., 71 N. Y. 593; Cecil Nat'l Bank v. Watsontown Bank, 105 U. S. 217.

[3] Excelsior, etc., Co. v. Lacey, 63 N. Y. 422; Lexington, etc., R. Co. v Bridges, 17 B. Mon. (Ky.) 556.

[4] See Park v. Thomas, 66 N. Y. 559; Van Dyck v. McQuade, 86 N. Y. 38; See Whittaker v. Amwell Nat'l Bank, 52 N. J. Eq. 400; Chamberlain v. Hugenot, etc., Co., 118 Mass. 532.

[5] Excelsior, etc., Co. v. Lacey, 63 N. Y. 422; Gratz v. Redd, 4 B. Mon. 178, 195; Scott v. Fire, etc., Co., 7 Paige N. Y. 198; Stringer's Case, L. R. 4 Ch. App. 475.

and under a belief that there were profits to divide, when in fact there were none, they might be reclaimed; because the stockholders who received them were not entitled to them and they had been paid over and received under the operation of a mutual mistake.''[1] But when dividends are wrongfully paid out of the capital the money can not be recovered by the corporation, although it may be by its creditors, or by its receiver acting in the rights of its creditors, and it is no defense to such an action that the directors acted in good faith in paying the dividend.[2] An officer of a corporation is bound to know its condition and has no right to receive a dividend unless it is legitimately earned. A dividend paid in violation of this rule may be reclaimed by an assignee of the insolvent corporation.[3] A stockholder who assents to the payment of a salary to an officer of the corporation in excess of that allowed by a resolution of the board of directors, can not participate in a dividend declared out of the funds resulting from the repayment by the officer of the excess.[4] Where the directors of a national bank placed a fictitious valuation on the assets in order to declare a stock dividend, they are liable to the receiver for the par value of the stock for the benefit of creditors.[5]

§ 410. **Set-off by the corporation.**—The rights of parties to dividends are fixed and determined at the time the dividend is declared.[6] The corporation may, therefore, retain dividends which have been apportioned to a stockholder, and set the amount off against a debt due from the stockholder to the corporation.[7] Thus, a bank which has no implied lien upon the

[1] Lexington, etc., Co. v. Page, 17 B. Mon. (Ky.) 412.

[2] Minnesota, etc., Co. v. Langdon, 44 Minn. 37. *Contra*, as to receiver of a national bank, McDonald v. Williams, 174 U. S. 397. See Lexington, etc., Co. v. Page, 17 B. Mon. (Ky.) 412, and Grant v. Ross (Ky.), 37 S. W. Rep. 263. The fact that the payment in question was made under authority of a resolution of stockholders is immaterial. Grant v. Ross (Ky.), 37 S.W. Rep. 263.

[3] Main v. Mills, 6 Biss. C. C. 98.

[4] Brown v. DeYoung, 167 Ill. 549, 47 N. E. Rep. 863.

[5] Cockrill v. Abeles, 86 Fed. Rep. 505.

[6] Gemmell v. Davis & Co., 75 Md. 546; § 404.

[7] Hagar v. Union Nat'l Bank, 63 Maine 509; Sargent v. Frank Ins. Co., 8 Pick. (Mass.) 90; Donnally v. Herndon, 41 W. Va. 519; King v. Pater-

shares of its stockholders may retain dividends actually declared, and apply the amount on the debt of the stockholder, as a dividend is simply so much money in its possession. But the corporation can not retain such money for a debt for which the stockholder is liable only as a surety, and which is not yet due.[1]

§ 411. **Who entitled to dividends.**—It has already been stated that the right to dividends is fixed at the time they are declared. They, therefore, belong to those who are stockholders at that time without reference to the time when the profits out of which the dividend is to be paid were earned.[2] "The purchaser of a share of stock in a corporation takes the stock with all its incidents, and among these is the right to receive all future dividends, that is, the proportionate share of all profits not then divided; and as we understand the law and the usage of such corporations, it is wholly immaterial at what time or from what sources these profits have been earned; they are an incident to the shares, to which the purchaser becomes at once entitled, provided he remains a member of the corporation until a dividend is made."[3] It is settled law that "dividends must be general on all the stock so that each stockholder will receive his proportionate share. The directors have no right to declare a dividend on any other principle. They can not exclude any portion of the shareholders from an equal participation in the profits of the company."[4]

(*a*) *As Between Successive Absolute Owners.*

§ 412. **In general.**—In ordinary transfers of stock nothing is said about dividends, and in the great majority of cases

son, etc., R. Co., 29 N. J. L. 504. Contra, Ex parte Winsor, 3 Story C.C. 411.

[1] Solomon v. First Nat'l Bank, 72 Miss. 851. See First Nat'l Bank v. De Morse (Tex.), 26 S. W. Rep. 417.

[2] Jones v. Railroad Co., 57 N. Y. 196; Goodwin v. Hardy, 57 Maine 143; March v. Eastern R. Co., 43 N. H. 515; Boardman v. Railroad Co., 84 N. Y. 157.

[3] March v. Eastern R. Co., 43 N. H. 515.

[4] Stoddard v. Foundry Co., 34 Conn. 542; Jones v. Railroad Co., 57 N. Y. 196. "The stockholders were all of the same class, and when such is the case the dividends must always be *pro rata*, equal and without preference." Hill v. Mining Co. (Mo.), 21 S. W. Rep. 508; Ryder v. Railroad Co., 13 Ill. 516.

they are governed by the usages of a stock exchange. Commonly the directors of a corporation resolve that dividends shall be declared from the profits of a certain period payable at a future day certain to those who are shareholders at that time; or at a certain period prior thereto when the transfer books of the corporation are closed. By the usage of the stock exchange all transfers made before the books are closed are "dividend-on" and all subsequent transfers "ex-dividend." These customs, however, have no application to transfers made elsewhere than on the stock exchange.[1] A transfer of stock carries with it ordinarily the right to all dividends declared after the transfer, although earned before the transfer. The right to such dividends passes as an incident of the stock.[2] But a dividend declared before the transfer, although payable after the transfer, belongs to the transferrer.[3] A dividend declared before the death of a testator becomes a part of the *corpus* of the estate, and goes to the executor.[4] Generally a corporation is protected if it pays a dividend to the person who appears as the owner of the stock on the corporate books, unless it has notice of the fact that the shares have been transferred.[5] If, however, it pays a dividend declared after the transfer to the transferrer, with knowledge of the transfer, it is liable to the transferee.[6]

[1] Lombardo v. Case, 45 Barb. (N.Y.) 95.

[2] Gemmell v. Davis & Co., 75 Md. 546; Boardman v. Railway Co., 84 N. Y. 157; Jermain v. Railway Co., 91 N.Y. 483; Phelps v. Farmers', etc., Bank, 26 Conn. 269; March v. Railway Co., 43 N. H. 515. One who sells stock, reserving the dividend that may be declared at a certain date, can not claim a stock dividend when declared. The reservation will be construed to apply to cash dividend only. Kaufman v. Woolen Mills Co., 93 Va. 673, 25 S. E. Rep. 1003; Charlottesville, etc., v. Mahan, 136 U. S. 548.

[3] Wheeler v. Sleigh Co., 39 Fed. Rep. 347; Hopper v. Sage, 112 N. Y. 530; In re Kernochan, 104 N.Y. 618; Bright v. Lord, 51 Ind. 272, 19 Am. Rep. 732. *Contra*, Burroughs v. Railway Co., 67 N. C. 376, 12 Am. Rep. 611.

[4] In re Kernochan, 104 N. Y. 618; De Gendre v. Kent, L. R. 4 Eq. 283; Wheeler v. Sleigh Co., 39 Fed. Rep. 347.

[5] Brisbane v. Railway Co., 94 N. Y. 204; Cleveland, etc., R. Co. v. Robbins, 35 Ohio St. 483.

[6] Gemmell v. Davis & Co., 75 Md. 546, 23 Atl. Rep. 1032; Robinson v. Bank, 95 N. Y. 637; Hill v. Mining Co., 124 Mo. 153, 21 S. W. Rep. 508; Central Nebraska Nat'l Bank v. Wilder, 32 Neb. 454, 49 N. W. Rep. 369, Guaranty Co., etc., v. East, etc., Co.,

§ 413. **Conditional sales and transfers.**—When an option is given to purchase shares within a certain period, or a sale is made upon a condition subsequent, and the sale is completed or the condition performed, the transfer dates from the time of the agreement and the purchaser is entitled to all dividends declared after that date. Thus, where the defendant sold his shares in a gas company on August 1st, on condition that twenty per cent. of the price should be paid before August 29th, and the condition was fulfilled, the purchaser was entitled to a dividend declared on August 28th. "The completion of the purchase," says the court, "has relation back to the time when the contract was made, which vested from that moment the right to the shares in the purchasers. They purchased the shares on that day and at that time and at their then value, and when they paid the remainder of the purchase-money at the time fixed for completion, they had a complete title to the shares, as they bought them on the first of August."[1] So, where a party on March 6th offered to sell shares to B., if he gave security by March 24th, which was done, it was held that B. was entitled to a dividend declared between such dates.[2] So, where A. sold to B. an option to take certain shares within a year, it was held that the agreement to sell, when consummated, was a sale *in presenti* and that the purchaser was entitled to dividends declared during the time.[3] But it has been held that where A. contracted before July 3d to sell shares of stock to B., at B.'s option, to be accepted by July 16th, on which day the stock was actually transferred to B., that a dividend declared on the stock July 3d belonged to A., although it was not to be paid till August 1st.[4]

96 Ga. 511, 23 S. E. Rep. 503; Armour v. Town Co., 98 Ga. 458, 25 S. E. Rep. 504.

[1] Black v. Homersham, L. R. 4 Exch. Div. 24.

[2] Harris v. Stevens, 7 N. H. 454.

[3] Currie v. White, 45 N. Y. 822.

[4] Bright v. Lord, 51 Ind. 272. But in Burrows v. North Carolina, etc., R. Co., 67 N. C. 376, 12 Am. Rep. 611, it is held that the sale of shares of stock carried with it dividends that are declared thereupon, although they are payable at a date subsequent to the transfer of the stock.

§ 414. **Transfers made between the date of declaration and payment.**—A shareholder has no legal title to the accumulated profits until they are divided, and there can be no apportionment of dividends between the successive owners of shares.[1] The right to dividends which have been declared belongs to the transferrer, and to those which are declared after the transfer, to the transferee. Incident to the ownership of stock in a corporation, and passing with the assignment of shares thereof, is the right to receive the proportional share of all the profits not divided at the time of the purchase of the shares; and it is immaterial at what time or from what source these profits have been earned.[2]

The declaration of a dividend is equivalent to a separation of the fund from the capital of the corporation. After it is credited to the shareholder the amount is separated from the assets; it is no longer represented by his shares and no longer an incident thereof, and when he transfers his shares, he does not transfer his dividend.[3]

(b) As Between Life Tenant and Remainder-Man.

§ 415. **General statement.**—Many difficult questions arise in determining the rights of dividends on stock as between successive owners of qualified interests. It is not uncommon for a testator to provide in his will that the income from certain shares of stock shall be paid to one person during his life and that after his death the absolute property in the stock shall pass to another person. In ordinary cases no difficulties arise, as the income on the shares goes to the life-tenant and the principal or capital passes unimpaired to the remainder-man. Ordinary

[1] Clapp v. Astor, 2 Edw. Chan. 379; Kane v. Bloodgood, 7 John. Ch. 90; Granger v. Bassett, 98 Mass. 462; Jones v. Ogle, L. R. 14 Eq. 419.

[2] March v. Eastern R. Co., 43 N. H. 515; Williams v. Tel. Co., 61 How. Pr. 216, 93 N. Y. 162; Hyatt v. Allen, 56 N. Y. 553; Jones v. Railway Co., 57 N. Y. 196; Boardman v. Railway Co., 84 N. Y. 157; Jermain v. Railway Co., 91 N. Y. 483; Ryan v. Leavenworth R. Co., 21 Kan. 365.

[3] Jermain v. Lake Shore R. Co., 91 N. Y. 483; Boardman v. Lake Shore R. Co., 84 N. Y. 157; Carpenter v. New York, etc., R. Co., 5 Abb. Pr. 277; Bright v. Lord, 51 Ind. 272. *Contra*, Burroughs v. North Carolina R. Co., 67 N. C. 376, 12 Am. Rep. 611.

dividends, that is, dividends payable out of net profits, go to the life-tenant. But when the corporation by reason of an increase of its capital or some unusual prosperity, declares an extraordinary dividend in the form of cash or stock, it is not easy to determine whether this shall be considered as income or capital. The authorities proceed upon different principles, and can not be reconciled. About the only principle which is conceded by all the cases is that the intention of the testator or the person creating the trust must govern, if it can be ascertained.[1] The courts in different jurisdictions have established three well-defined rules. (1) The English rule by which ordinary cash or stock dividends belong to the life-tenant, and extraordinary cash or stock dividends form a part of the corpus and go to the remainder-man. (2) The Massachusetts rule, or the rule in Minot's case, which treats cash dividends whether great or small as income for the life-tenant, and stock dividends whenever earned or declared, as capital for the remainder-man. And (3) the Pennsylvania rule, or as it is sometimes called the American rule, under which the court inquires as to the time when the fund out of which the extraordinary dividend in question is to be paid, was earned or accumulated; and gives that to the remainder-man which was earned before the life estate began without reference to the time when declared or payable.

§ 416. **The English rule.**—The English rule which gives to the life tenant all ordinary dividends whether cash or stock, and to the remainder-man all extraordinary dividends, would seem to be somewhat modified by later decisions holding that the court would be largely governed by the intention of the corporation.[2] In the early case of Brander v. Brander,[3] it was held that where government annuities were received by a bank in exchange for a subscription of funds to the public

[1] McLouth v. Hunt, 154 N. Y. 179, 39 L. R. A. 230; Spooner v. Phillips (Conn.), 16 L. R. A. 461.

[2] Price v. Anderson, 15 Sim. 473; Sproule v. Bouch, L. R. 29 Ch. Div. 635, 653.

[3] Brander v. Brander, 4 Ves. Jr. 800; Irving, etc., v. Honstoun, 4 Paton (Scotch) App. Cas. 521.

service and divided among the shareholders of the bank, they went to the remainder-man, and the income from them to the life-tenant. In one case it was held that there was no distinction between cash and stock dividends,[1] and that all extraordinary bonuses go to the remainder-man and all ordinary dividends to the life-tenant, although they were increased from time to time according to earnings.[2] In a recent case in New York,[3] the court said: "It is impossible to read the English cases without being impressed with the statement of the judges, so often repeated, that they found great difficulty in formulating any principle upon which the decisions rested. An attempt to give a reason for the rule was made in one of the more recent cases, but without much success.[4] It was all summed up in the end by the court in a single sentence, 'What the company says is income shall be income, and what it says is capital shall be capital.'"

§ 417. **The Massachusetts rule.**—The underlying principle of this rule, which recognizes all *cash* dividends as income and all *stock* dividends as capital, is recognized in Massachusetts, Georgia and Connecticut. It was first established in Minot v. Paine,[5] and has since been adhered to with some modifica-

[1] Paris v. Paris, 10 Ves. Jr. 185.

[2] Barclay v. Wainwright, 14 Ves. Jr. 67.

[3] McLouth v. Hunt, 154 N. Y. 179, 39 L. R. A. 230.

[4] Sproule v. Bouch, L. R. 29 Ch. Div. 635.

[5] Minot v. Paine, 99 Mass. 101, 96 Am. Dec. 705; Spooner v. Phillips, 62 Conn. 62, 16 L. R. A. 461. See, also, Rand v. Hubbell, 115 Mass. 461, 15 Am. Rep. 121; Millen v. Guerrard, 67 Ga. 284. In McLouth v. Hunt, 154 N. Y. 179, 39 L. R. A. 230, the court said: "The appeal is sought to be sustained first by a class of cases in England, founded upon Brander v. Brander, 4 Ves. Jr. 800, and followed in Irving, etc., v. Houstoun, 4 Pat. App. 521; Paris v. Paris, 10 Ves. Jr. 185; In re Barton's Trust, L. R. 5 Eq. 238. Apart from the evident inclination of the judicial mind of that day, in that country, to favor entails, perpetuities, and accumulations of property, it can hardly be said that these cases were well considered. Lord Chancellor Eldon admitted this in Paris v. Paris, 10 Ves. Jr. 185, where he said: 'I confess I don't think I can safely rest upon any distinction between this case and those that have been determined. I have had great difficulty in stating the principle that led to them. But in the case from Scotland great inquiry was made as to the length to which practice had carried the decisions here, and at the rolls, and as it appeared that it had gone to great

tions.[1] Under this rule, the courts will not enter upon an original inquiry for the purpose of ascertaining the source of such

length, the house of lords did not think it proper to disturb that.' Then, proceeding to notice the argument now made in this case, that there is a distinction between stock and cash dividends, he disposes of that contention with a homely but expressive remark. He said: 'As to the distinction between stock and money, that is too thin; and if the law is that this extraordinary profit, if given in the shape of stock, shall be considered capital, it must be capital if given in money.' The rule, as thus established in England, was followed in Massachusetts, more as one of convenience than of justice, in a line of cases that are not quite consistent with each other. Minot v. Paine, 99 Mass. 101, 96 Am. Dec. 705; Daland v. Williams, 101 Mass. 571; Leland v. Hayden, 102 Mass. 542; Heard v. Eldredge, 109 Mass. 258, 12 Am. Rep. 687; Rand v. Hubbell, 115 Mass. 461, 15 Am. Rep. 121; Davis v. Jackson, 152 Mass. 58, 23 Am. St. Rep. 801. The rule was adopted there mainly upon the authority of the early English cases to which reference has been made. The supreme court of the United States laid down the same rule in Gibbons v. Mahon, 136 U. S. 549, evidently following the doctrine of the English and Massachusetts cases. See note to Goodwin v. Hardy, 99 Am. Dec. 758."

[1] Thus, in Heard v. Eldridge, 109 Mass. 258, and Rand v. Hubbell, 115 Mass. 461, it was held that if the dividend is merely the result of pre-existing capital of the corporation, as where a part of its property is taken in the exercise of the power of eminent domain, and the money received is distributed as dividends, it belongs to the remainder-man. See note to 14 Am. St. Rep. 633. In Thomas v. Gregg, 78 Md. 551, the court said of the Massachusetts rule: "This rule has not been altogether acceptable, and has been somewhat qualified, or modified, by subsequent cases in that state, although the general principle, as settled in Minot v. Paine, is still maintained. In Daland v. Williams, 101 Mass. 571, the directors having voted to increase the capital stock by 3,000 shares, declared a cash dividend of 40 per cent. and authorized the treasurer to receive that dividend in payment for 2,800 shares, the remaining 200 shares to be sold. The court held that the transaction was virtually a stock dividend, and that the shares must go to the remainder-man's fund. In Leland v. Hayden, 102 Mass. 542, where the company had invested its surplus earnings in its own stock, and subsequently declared a dividend of that stock, the life-tenant was held entitled to it. The Massachusetts court in these later cases determined that they can, in deciding whether in a given case the distribution is a stock or cash dividend, consider the actual and substantial character of the transaction, and not its nominal character only. See, also, Rand v. Hubbell, 115 Mass. 461; Heard v. Eldredge, 109 Mass. 258; Davis v. Jackson, 152 Mass. 58." In Rand v. Hubbell, Ch. J. Gray, in speaking of the earnings of a corporation, said: "When a distribution of said earnings is made by the corporation among its stockholders, the question whether such distribution is an apportionment of additional stock or a division of profits, depends on the substance and intent of the action of the corporation, as shown by its votes."

dividends, but will consider the proceedings of the corporation to determine whether it and its trustees regarded an extraordinary dividend in question as profits or as capital, and will treat it as the corporation treated it. If the corporation declares it to be profits, it will belong to the owner of the life estate, and if, on the other hand, the corporation was apparently making an increase in the capital stock to adequately represent pre-existing assets, the remainder-man is entitled to the increase.[1] The intention of the corporation is thus made the test. This rule is adopted by the supreme court of the United States, which, after stating the rule that the directors may determine what disposition shall be made of profits, says:[2] "Whether the gains and profits of a corporation should be so invested and apportioned as to increase the value of each share of stock for the benefit of all persons interested in it, either for a term of years or for life, or by way of remainder in fee, or should be distributed and paid out as income, to the tenant for life or for years, excluding the remainder-man from any participation therein, is a question to be determined by the action of the corporation itself, at such times and in such manner as the fair and honest administration of its whole property and business may require or permit."

In Rhode Island it was held that new shares of corporate stock resulting from a distribution of surplus earnings, and distributed to stockholders, are capital and go to the remainder-man.[3] The corporation during the life of the life-tenant distributed new shares in conformity to the recommendations of a committee, which recited that "the contingent fund of the corporation, which to a great extent has already gone into the construction of the road, the virtual extinguishment of the debt of $1,000,000 to the city of Albany by the sinking fund providing for its payment, releasing the income of the road from the payment of interest on these bonds, and contribution to the fund,

[1] Rand v. Hubbell, 115 Mass. 461, 15 Am. Rep. 121.

[2] Gibbons v. Mahon, 136 U. S. 549, quoted in Spooner v. Phillips, 62 Conn. 62, 16 L. R. A. 461. This is practically the English rule. The intention of the corporation to declare a dividend as such must govern. See § 416.

[3] Petition of Brown, 14 R. I. 371.

aside from other considerations which might well be urged, fully require, as in justice to the stockholders, that twenty thousand new shares shall be issued and distributed." The court said: "The only question necessary now to be decided is whether shares of stock distributed to the stockholder of a corporation are to be taken as income and belong to the life-tenant. We think they are not to be so taken. Such a distribution of shares is in no proper sense a dividend. The surplus property of the corporation which is represented by such stock is still retained by the corporation, and managed and applied in the prosecution of the business. Nor is the value of the stock held by any individual stockholder in anywise changed by such a distribution. He has a greater number of shares, but each share is of proportionately less value." Where a dividend of $25 for each share of its capital stock is declared by a corporation, and any stockholder who wishes is entitled to take an additional share of stock for every four shares of stock held by him instead of receiving his dividend in money, and the earnings of the corporation are sufficient to pay the dividend but if used for that purpose then it will become necessary to raise an equal amount to pay for the additions which have been made to the capital, and which had increased its value above the par value of the stock, the dividend must be treated as income, and not capital.[1] Shares which are issued to represent the increase in the value of the property of the corporation, which was caused by the development of its business and which does not represent ordinary surplus earnings, constitute capital and not income, and go to the remainderman-man.[2]

§ 418. **The Pennsylvania rule.**—What is known as the Pennsylvania rule was established in Earp's Appeal,[3] and has been so generally adopted that it is sometimes called the American rule. The underlying principle is found in the statement that the court will award the thing distributed regardless of its form to whoever is entitled to it. The object in all

[1] Davis v. Jackson, 152 Mass. 58, 23 Am. St. Rep. 801.

[2] Spooner v. Phillips, 62 Conn. 62, 16 L. R. A. 461.

[3] Earp's Appeal, 28 Pa. St. 368.

cases is to keep the increase in the capital for the remainderman and the increase in the income for the life-tenant.[1] When necessary to determine what is in fact capital and what income, the court will investigate the facts in order to learn the source from which the fund came, and distribute it regardless of the name by which the corporation called it or the form in which it is distributed. Thus, when a corporation, having actually made profits, proceeds to distribute such profits amongst the stockholders, the tenant for life would be entitled to receive them, and this without regard to the form of the transaction. Equity which disregards form and grasps the substance would award the thing distributed, whether stock or moneys, to whomsoever was entitled to the profits.[2] In the leading case[3] it appeared that the estate of Earp, who died in November, 1848, embraced stock in a manufacturing company upon which large surplus profits over and above the current dividends had accumulated, both before and after his decease. In July, 1854, the capital stock was increased from $200,000 to $500,000 by creating 6,000 additional shares of $50 each; which were paid for out of the accumulations. At the testator's death these surplus profits were nearly $300,000, and the stock issued had increased to $700,000. The market value of the stock at his death was $125 per share. When the new stock was issued its value was $80. The number of shares belonging to the estate was 1,350 instead of 540. As the new shares were therefore in part paid from the surplus existing at the death of Robert Earp, and partly from the accumulations after his death, they were properly apportioned between the life-tenant and those entitled to the remainder. It was held (1) that the surplus property accumulated at the death of the testator as respects the estate was essentially part of the stock itself, and was subject to the trust in the will as so much principal; and (2) that the accumulations after his decease when they came to be divided were income in like manner as the cur-

[1] Oliver's Est., 136 Pa. St. 43, 20 Am. St. Rep. 894, note.

[2] Moss' App., 83 Pa. St. 264, 24 Am. Rep. 164.

[3] Earp's Appeal, 28 Pa. St. 368.

rent dividends, and therefore belonged to the life-tenant, no matter whether the division or distribution thereof was in cash, scrip or stock.

In another case[1] it appeared that there was no division of surplus profits or of earnings accumulated either before or after the death of the testator, but that the transaction was simply an increase of stock to the stockholders upon payment of the price at par, and $10 per share additional to go to the surplus fund. The market value of the old shares was not shown to have varied between the death of the testatrix and the issue of the new stock, but a slight decrease occurred after the issue. Instead of subscribing to the new issue the executor sold the privilege, and the question was whether the sum realized should be treated as income or principal. The court said: "The entire value of the stock, with all its incidents, at the death of the testatrix constituted the principal of the estate. On this principal the appellant was entitled to the income, whatever value beyond par the stock then had by reason of the large surplus fund of the company, or otherwise, attached to the stock and formed a part of the principal. The appellant was not given any part of this aggregated value of the stock; the income therefrom was all she was entitled to receive. Whatever was capital must remain capital." When corporate stock is by the will of a deceased given in trust, the income thereof for the use of the beneficiary for life, with remainder over, the surplus profits which have accumulated in the life-time of the testator, but which have not been divided until after death, belong to the *corpus* of the estate. The dividends from earnings made after his death are income, payable to the life-tenant, whether they are cash, scrip or stock.

The profits of a sale of new stock issued after the testator's death, in lieu of profits applied to the improvement of the corporate property in the testator's life-time, is capital and not income, and belongs to the *corpus*.[2]

[1] Biddle's App., 99 Pa. St. 278.

[2] Estate of Smith, 140 Pa. St. 344, 23 Am. St. Rep. 237.

§ 419. **The general adoption of this rule.**—Notwithstanding the simplicity of the rule in Minot's case and the fact that it has been accepted by the supreme court of the United States, the Pennsylvania rule has been generally adopted in recent cases. Although it is more difficult to apply, the results are more generally in accord with justice and the intent of the testator. For some time there was doubt as to the position of the New York court of appeal,[1] although the lower court had repudiated the English and Massachusetts doctrine,[2] but New York,[3] along with New Jersey,[4] New Hampshire,[5] Kentucky,[6] Maryland[7] and Tennessee,[8] has now adopted the Pennsylvania rule. With reference to the rule that what the company says is income shall be income, the New York court said:[9] "This is but another way of saying that whether accumulated earnings belong to the life-tenant or the remainder-man depends upon the action of the corporation, and that the property rights of such parties under the will are governed by the mere form of capitalization; that the majority of the board of directors may give them to one or the other at their will. While such a rule might have the merit of simplicity and convenience, it ought not to determine the property rights of parties interested in the corporate property. That a testamentary provision of this character, for the benefit of both the life-tenant and the remainder-man, who are generally the nearest

[1] Riggs v. Cragg, 89 N. Y. 479.

[2] Clarkson v. Clarkson, 18 Barb. 646; Riggs v. Cragg, 26 Hun 89; Simpson v. Moore, 30 Barb. 637; Goldsmith v. Swift, 25 Hun 201.

[3] McLouth v. Hunt, 154 N. Y. 179, 39 L. R. A. 230.

[4] Van Doren v. Olden, 19 N. J. Eq. 176, 97 Am. Dec. 650. In Lang v. Lang's Exrs. (N. J.), 41 Atl. Rep. 705, the court said: "The underlying principle applicable to this case is that no corporate dividend, declared after the right to the dividend has become severed from the ultimate ownership of the stock upon which such dividend is declared, belongs in equity to the person entitled to income, except so far as it is derived from the earnings of the stock after such severance. The general trend of judicial opinion in this country is toward the adoption of this principle, and we adopt it without qualification."

[5] Lord v. Brooks, 52 N. H. 72.

[6] Hite v. Hite, 93 Ky. 257, 19 L. R. A. 173.

[7] Thomas v. Gregg, 78 Md. 545.

[8] Pritchitt v. Nashville, etc., Co., 96 Tenn. 472, 33 L. R. A. 856.

[9] McLouth v. Hunt, 154 N. Y. 179, 39 L. R. A. 230.

and dearest objects of the testator's bounty, can in this way be voted up or down, increased or diminished, as the corporation may elect, and that such action precludes the courts from looking into the real nature and substance of the transaction and adjusting the rights of the parties, according to justice and equity, is a proposition that can not be accepted. The mere adoption by the corporation of a resolution can not change accumulated earnings into capital as between the life-tenant and remainder-man."[1] A corporation passed a resolution reciting that for the three fiscal years, ending September 30, the net earnings of the company had amounted to a certain sum, that it had been used, among other things, for the permanent improvement of the railway and for new construction, and that, therefore, a dividend of twenty per cent. be declared for said period, "payable in common stock of the company."

This dividend was held to be income and not capital and to go to the life-tenant. It was said that when it is possible for the court to ascertain, with any certainty, whether the distribution of the stock dividend includes net earnings, and, if so, what proportion, and also whether such earnings were intended to be made a part of the capital or merely to be used temporarily, with the intention on the part of the directors of refunding them to the shareholders as income, it is the duty of the court to make such investigations and dispose of the stock in an equitable way between the life-tenant and remainder-man.[2]

II. Actions by Stockholders.

§ 420. **Actions against third persons—The protection of collective rights.**—The collective rights of a member are such as he enjoys within the corporation. They are rights in the corporate concern, rather than against it, and should be enforced through the corporate organization. It is the duty of

[1] In Gibbons v. Mahon, 136 U. S. 549, Mr. Justice Gray, after an examination of the authorities, concludes that the weight of authority supports the proposition that the intent of the corporation as manifested by its vote or resolution governs. See, also, Richardson v. Richardson, 75 Maine 570, 46 Am. Rep. 428.

[2] Thomas v. Gregg, 78 Md. 545.

the corporation and not of the shareholder[1] to protect the corporate rights,[2] but when the proper officers are unable or unwilling to act the corporation can not act, and it is necessary to permit the members to sue for the protection of their equitable interests.[3] For fraudulent and wrongful dealing with corporate property, prejudicially affecting the interests of the corporation, and hence the interests of the shareholders, the right of action is primarily in the corporation, and is to be asserted by it rather than by individual stockholders, unless it is shown to be impracticable for the complaining stockholder to induce the corporation to sue.[4] The cases in which the stockholders will be permitted to maintain an action which should ordinarily be brought by the corporation, are generally brought to prevent a threatened injury, although it may be to recover damages for injuries already suffered.[5]

[1] Silk, etc., Co. v. Campbell, 27 N. J. L. 539; Henry v. Elder, 63 Ga. 347; VanKirk v. Adler, 111 Ala. 104.

[2] Bradley v. Richardson, 2 Blatchf. (C. C.) 343.

[3] Flynn v. Brooklyn, etc., R. Co., 158 N. Y. 493; Brinckerhoff v. Bostwick, 88 N. Y. 52.

[4] Hodgson v. Duluth, etc., R. Co., 46 Minn. 454; Hutton v. Joseph Bancroft & Sons Co., 83 Fed. Rep. 17; Dunphy v. Travelers', etc., Assn., 146 Mass. 495; Holton v. Newcastle R. Co., 138 Pa. St. 111; Rothwell v. Robinson, 39 Minn. 1; Doud v. Wisconsin, etc., R. Co., 65 Wis. 108. In Pomeroy Eq. Jur., § 1094, it is said: "In cases belonging to this class, therefore, whatever be the nature of the particular wrong, whether intentional and fraudulent, or resulting from negligence or want of reasonable prudence, and whatever be the indirect loss occasioned to individual stockholders, no equitable suit for relief against the wrong-doing directors or officers can be maintained by a stockholder or stockholders individually, nor by a stockholder suing representatively on behalf of all others similarly situated, unless the special condition of circumstances exists to be described in the next following paragraph, namely, that the corporation either actually or virtually refuses to prosecute. Even if the stockholder alleges that the value of his own stock has been depreciated by the defendants' acts, or that he has sustained other special damage, he is not thereby entitled to maintain the suit." Oswald v. St. Paul, etc., Co., 60 Minn. 82, 61 N. W. Rep. 902.

[5] Chicago v. Cameron, 120 Ill. 447. See Samuel v. Holladay, 1 Woolw. 400; Carter v. Ford, etc., Co., 85 Ind. 180. As to the right of a minority stockholder to an injunction to prevent the voting of exorbitant salaries to officers, see Decatur, etc., Co. v. Palm, 113 Ala. 531, 59 Am. St. Rep. 140.

§ 421. **When a stockholder may sue.**—The relation between the corporation and its members is similar to that of trustee and beneficiaries, and the beneficiaries under a trust are not entitled to sue for the protection of the trust unless the trustee has refused or is unable to protect it.[1] A shareholder is entitled to relief in a court of equity on account of any infringement of his equitable rights as member and beneficiary of the corporation: Provided, first, that the corporation itself be unable, by reason of the default of its agents, to obtain an adequate remedy within a reasonable time; and, secondly, that the right to obtain redress for an injury be not implicitly relinquished by the shareholder to the discretion of the regular agents of the corporation as a mutual concession for the sake of peace and good-will.[2]

It must be made to appear to the court that the shareholder will suffer irremediable loss if not permitted to maintain the suit,[3] and that a real effort has been made to induce the proper officers to bring the suit,[4] and that their refusal to act is a breach of trust, and not a mere error of judgment.[5] The demand must be made, although the term of corporate existence has expired, when the corporation is by the statute kept alive for the purpose of winding up its business.[6] But when the officers have absconded, and the corporation is practically dissolved, a stockholder may maintain a suit against a person to whom the corporate property has been fraudulently conveyed.[7]

The rule that the stockholder can not maintain an action against one who has injured the corporation does not apply where the acts are not only wrongs against the corporation,

[1] Western R. Co. v. Nolan, 48 N. Y. 513.

[2] Republican, etc., Co. v. Brown, 19 U. S. App. 203, 24 L. R. A. 776; Russell v. Wakefield, etc., Co., L. R. 20 Eq. 474; Dodge v. Woolsey, 18 How. (U. S.) 331; Loftus v. Farmers', etc., Assn., 8 S. Dak. 201; Memphis City v. Dean, 8 Wall. (U. S.) 64; People v. State Treasurer, 24 Mich. 468; Mount v. Radford, etc., Co., 93 Va. 427; Rogers v. Nashville, etc., R. Co., 91 Fed. Rep. 299.

[3] Detroit v. Dean, 106 U. S. 537.

[4] Dimpfell v. Ohio, etc., R. Co., 110 U. S. 209.

[5] Hawes v. Oakland, 104 U. S. 450; Rathbone v. Gas Co., 31 W. Va. 798.

[6] Taylor v. Holmes, 127 U. S. 489.

[7] Wilcox v. Bickel, 11 Neb. 154.

but also a violation of a duty owed directly to the individual stockholder. Thus, where the stockholder pledged his stock as collateral with the directors of the corporation, and the latter entered into a conspiracy to depreciate the value of the stock for the purpose of buying it in at less than its value, it was held to be a wrong against both the corporation and the stockholder, and that the action could be maintained by the stockholder. Taft, J., said:[1] "It is undoubtedly true, as the circuit court held, that a stockholder, merely as such, can not have an action on his own behalf against one who has injured the corporation, however much the wrongful acts may have depreciated the value of his shares, but we are of opinion that this principle has no application where the wrongful acts are not only wrongs against the corporation, but are also violations by the wrong-doer of a duty arising from contract or otherwise, and owing directly by him to the stockholders."[2]

§ 422. **Conditions precedent to right of action.**—Before an action can be maintained by a stockholder it must appear

(1) That no agents of the corporation having the requisite authority are willing or able to act;[3] *and*

(2) That a demand has been made upon them and that they have refused to act;[4] *or*

[1] Ritchie v. McMullen, 79 Fed. Rep. 522, 25 C. C. A. 50.

[2] Smith v. Hurd, 12 Metc. (Mass.) 371; Allen v. Curtis, 26 Conn. 456; Wallace v. Bank, 89 Tenn. 630; Conway v. Halsey, 44 N. J. L. 462; Porter v. Sabin, 149 U. S. 473.

[3] Bill v. Western Union, etc., Co., 16 Fed. Rep. 14; Hawes v. Oakland, 104 U. S. 450, Wilgus' Cases.

[4] Memphis City v. Dean, 8 Wall. 64; Detroit v. Dean, 106 U. S. 537; Hawes v. Oakland, 104 U. S. 450; Shawhan v. Zinn, 79 Ky. 300; Roman v. Woolfolk, 98 Ala. 219; Forrester v. Boston, etc., Co. (Mont.), 55 Pac. Rep. 229; Smith v. Dorn, 96 Cal. 73; Albers v. Merch. Exch., 45 Mo. App. 206. A demand is not necessary where the corporation long since ceased to do business and the directors are unknown. Tennessee, etc., Co. v. Ayers, 43 S. W. Rep. 744. "The right to sue and be sued, to maintain and defend actions concerning corporate rights and corporate liabilities, is a power incident to every corporation, * * * and with this right of the corporation to maintain and defend actions concerning its corporate rights or liabilities the stockholder can not interfere except when the directors refuse to act or are guilty of fraud in the maintenance or defense of the action."

(3) That the agents themselves are the authors of the wrong.[1] Under such circumstances, no demand to bring suit is required as "the law does not require the minority stockholders to do so absurd a thing as a condition of seeking relief against the wrongful acts of the directors and majority stockholders."[2]

§ 423. **Exceptions to the rule.**—To the general rule above stated there are two exceptions:

(1) Equity will not interfere if the acts of the managing agents are within the ratifying power of the majority.[3] But this exception has no application where the act complained of is in excess of the power of the majority,[4] or where the relief sought is merely preventive.

(2) Equity will not interfere unless it appears that a delay of the remedy until a corporate meeting can be held and the guilty agents removed would unduly prejudice the rights of the complainants, or that delay would be useless.[5]

§ 424. **Illustrations, Foss v. Harbottle.**[6]—Two members of an incorporated company, called the Victoria Park Company, filed a bill against the directors thereof, charging them with a variety of fraudulent, illegal acts, whereby the property of the company was misapplied, aliened and wasted, and praying that the defendants might make good to the company the damages by reason of the acts complained of, and that a receiver might be appointed to apply the property of the company in discharge of its liabilities; and to secure the surplus. The general result of the act of incorporation was to make the directors a governing body subject to the strict control of the proprietors, who had power, when assembled in general meeting, to originate

Baines v. Babcock, 95 Cal. 581, 27 Pac. Rep. 674; Greaves v. Gouge, 69 N. Y. 154; Brewer v. Boston Theater, 104 Mass. 378; Ware v. Bazemore, 58 Ga. 316.

[1] Peabody v. Flint, 6 Allen 52; Excelsior, etc., Co. v. Brown, 74 Fed. Rep. 321, 42 U. S. App. 55.

[2] Bjorngaard v. Goodhue Co. Bank, 49 Minn. 483; Rothwell v. Robinson, 39 Minn. 1; Gerry v. Bismark Bank, 19 Mont. 191.

[3] Foss v. Harbottle, 2 Hare 461.

[4] Bagshaw v. Eastern, etc., R. Co., 7 Hare 114.

[5] Mozley v. Alston, 1 Ph. Ch. 790.

[6] Foss v. Harbottle, 2 Hare 461.

proceedings for any purpose within the scope of the company's powers, as well as to control the directors in any act which they might have originated. The court was of the opinion that the acts of the defendants complained of were of such a nature as to be capable of confirmation by the majority of the members of the company; that it did not appear that any attempt had been made to bring these acts before a general meeting of the shareholders; and that under these circumstances, the court could not interfere at the suit of a minority, whatever it might have been induced to do had proper means been resorted to and found ineffectual to set the general body of shareholders in motion.

§ 425. **Mozley v. Alston.**[1]—A bill was filed by two shareholders of a railroad company, against the company and its directors, alleging that the latter had been illegally appointed; that they had possession of the seal of the corporation, and that they were about to use it for various improper purposes. The bill prayed that the directors, who were the defendants, might be restrained from acting as directors, and be ordered to place the seal and the books and documents of the company under control of the lawful directors. It appeared from the statements in the bill that the majority of the shareholders agreed with the plaintiffs in their view of the illegality of the directors' appointment, and the court held that if they were so there was nothing to prevent the company from filing a bill in its corporate character to remedy the alleged violations, and that as the complainants showed no reasons to justify them alone in applying for redress, they were not entitled to its assistance.

§ 426. **Hawes v. Oakland.**[2]—This is probably the leading case upon this subject in the United States. A shareholder in a water-works company filed a bill in equity against the city, the corporation and its directors, and alleged that the company was furnishing the city with water free of charge

[1] Mozley v. Alston, 1 Ph. Ch. 790.

[2] 104 U. S. 450. Approved in Detroit v. Dean, 106 U. S. 537.

beyond what the law required it to do, and that the directors, contrary to his request, continued to do so to the great injury of himself, the other shareholders and the company. The court held that before the action could be maintained by the shareholder there must be shown :

1. Some action or threatened action of the directors or trustees, which is beyond the authority conferred by the charter or the law under which the company was organized; or,

2. Such a fraudulent transaction completed or threatened by them, either among themselves or with some other party, or with shareholders, as will result in serious injury to the company or the other shareholders; or,

3. That the directors, or a majority of them, are acting for their own interest in a manner destructive of the company, or of the rights of other shareholders; or,

4. That the majority of shareholders are oppressively and illegally pursuing in the name of the company a course in violation of the rights of the other shareholders, which can only be restrained by a court of equity.

5. It must also be made to appear that the complainant made an earnest effort to obtain redress at the hands of the directors and shareholders of the corporation, and that the ownership of the stock was vested in him at the time of the transactions of which he complains, or was thereafter transferred to him by operation of law.

§ 427. **The rights of transferees.**—A transferee of shares acquires the rights of the transferrer, and the right of action passes with the shares whether it was known to the transferee or not. If he is a purchaser in good faith without notice that the transferrer had precluded himself from suing by acquiescence, he may maintain the suit, as "it can never be held that the acquiescence of the original holder of stock in illegal acts of the directors of a company will bind a subsequent holder of that stock to submit to all future acts of the same character."[1]

[1] Bloxam v. Metropolitan R. Co., L. R. 3 Ch. App. 337. As to the practice in federal courts, see Equity Rule 9, printed in the preface to vol. 101, U

§ 428. **Discretionary power.**—But the courts will not control the discretionary powers of the managing agents of a corporation so long as they act honestly and within the power conferred by the charter.[1] Thus, directors will not be compelled to bring an action in the name of the corporation or pay dividends, unless there is abuse of discretion.[2]

§ 429. **Acquiescence.**—Neither the corporation nor the shareholders can repudiate an unauthorized transaction after the shareholders have acquiesced in the transaction and allowed the corporation to appropriate the benefits thereunder, but the acquiescence of a number or even of the majority will not bar a suit by the corporation, and the benefits of the proceeding will accrue to all the members. Where the individual member, who himself acquiesces in the wrong, is disqualified from suing, he, nevertheless, is entitled to share in the benefits of the proceeding by the corporation.

§ 430. **Parties to the suit.**—The suit may be brought by the holder of a single share, or all shareholders may join. If it is brought by a part only, it should purport to be on behalf of the plaintiffs and all others similarly situated. The corporation and all shareholders who are parties to the wrong complained of should be made defendants.[3] It is essential that the corporation should be made a party defendant.[4]

§ 431. **Right to restrain ultra vires acts.**—A stockholder who has not waived or forfeited his rights[5] may maintain a suit to restrain the corporation from doing an act which is *ultra vires*,[6] such as performing an illegal contract,[7] diverting

S. Rep., and comments of Mr. Justice Miller in Hawes v. Oakland, 104 U. S. 450; *supra*, § 296.

[1] §400; Oglesby v. Attrill, 105 U.S. 605.

[2] Samuel v. Holladay, 1 Woolw. 400.

[3] Davenport v. Dows, 18 Wall. 626; Davis v. Peabody, 170 Mass. 397.

[4] Shawhan v. Zinn, 79 Ky. 300; Dodge v. Woolsey, 18 How. (U. S.) 331; Memphis, etc., Co. v. Williamson, 9 Heisk. (Tenn.) 314.

[5] Dimpfell v. Ohio, etc., R. Co., 110 U. S. 209; Rabe v. Dunlap, 51 N. J. Eq. 40, 25 Atl. Rep. 959; Jefferson County Sav. Bank v. Francis, 115 Ala. 317.

[6] Carson v. Gaslight Co., 80 Iowa 638; Stewart v. Erie, etc., Co., 17 Minn. 372, Gil. 348; Dodge v. Woolsey, 18 How. (U. S.) 331.

[7] Morrill v. Boston, etc., R. Co., 55 N. H. 531.

the corporate funds to unauthorized purposes,[1] or entering upon a business not authorized by the charter.[2] A single stockholder who acts promptly may enjoin the corporation from accepting a legislative amendment which would substantially alter the corporate charter.[3] But the rule is otherwise if the charter was subject to amendment under the law in force when it was granted.[4] A minority stockholder can not invoke the jurisdiction of equity for himself and those who may subsequently join him to prevent the majority stockholders from making a contract which is neither *ultra vires* nor fraudulent.[5] A court of equity will not attempt to adjust controversies which have arisen among shareholders and directors relative to the proper mode of conducting the corporate business.[6] Equity will relieve the minority against the action of a majority stockholder who also holds a majority of the mortgage bonds in using the income for improper purposes and declining to accept traffic from other roads which would produce a fund to pay interest due, by which the corporation is to be forced into insolvency and its property sold for the purpose of enabling the majority stockholder to acquire title.[7]

The right to relief may be lost by acquiescence or delay. The business of a corporation was a failure and it was heavily in debt. Its plant was unsalable, and the directors, with the approval of all the shareholders but the plaintiff, acting in good faith, exchanged the plant for the paid-up shares of another corporation which was authorized to engage in the same business. The plaintiff knew of the transaction immediately after its completion and made no objection until more than two years had elapsed. He then brought an action against the corporation and the directors to recover the proportionate share of the property transferred, and the court held that, as-

[1] Rothwell v. Robinson, 39 Minn. 1; March v. Railway Co., 43 N. H. 515; Ashton v. Dashaway Assn., 84 Cal. 61; Central R. Co. v. Collins, 40 Ga. 582.

[2] Cherokee, etc., Co. v. Jones, 52 Ga. 276.

[3] Mowrey v. Indianapolis, etc., R. Co., 4 Biss. (C. C.) 78. § 186, *infra*.

[4] Mower v. Staples, 32 Minn. 284.

[5] Shaw v. Davis, 78 Md. 308, 23 L. R. A. 294.

[6] Republican, etc., Co. v. Brown, 19 U. S. App. 203, 24 L. R. A. 776.

[7] DeNeufville v. New York, etc., R. Co., 81 Fed. Rep. 10, 51 U. S. App. 374.

suming that the transfer was *ultra vires*, the plaintiff could not recover, on the ground that "It is inequitable for a stockholder, knowing that an act done by the directors and a majority of the stockholders, in good faith, for the benefit of the corporation, is in fact unauthorized, to apparently acquiesce by his silence, but secretly reserve an option to repudiate the act in case of loss, or to enjoy its benefits if it proves profitable.'"[1]

§ 432. **Control by the majority.**—The right to control the actions of the corporation in carrying out the objects set forth in the charter is vested in the majority of the stockholders, and the court will not, so long as the action is legal, interfere with the management at the instance of a minority stockholder.[2] A court of equity will interfere with this control at the instance of a minority stockholder only when absolutely necessary for the attainment of justice and the prevention of actual fraud.[3] Each and every stockholder contracts that the will of the majority shall govern in all matters coming within the limits of the act of incorporation. In cases involving no breach of trust, but only error or mistake of judgment on the part of directors who represent the corporation, individual stockholders have no right to appeal to the courts to dictate the line of policy to be pursued by the corporation.[4] "We suppose it to be stated as an indisputable proposition," says Chief Justice Bigelow, "that every person, who becomes a member of a corporation aggregate by purchasing and holding shares, agrees, by necessary implication, that he will be bound by all acts and proceedings within the scope of the powers and authority conferred by the charter, which shall be adopted and sanctioned by a vote of the majority of the corporation, duly taken and ascertained according to law. This is the unavoidable result of the fundamental principle that the

[1] Pinkus v. Minneapolis Linen Mills, 65 Minn. 40.

[2] Durfee v. Old Colony, etc., R. Co., 5 Allen (Mass.) 230; Hawes v. Oakland, 104 U. S. 450; Oglesby v. Attrill, 105 U. S. 605; Shaw v. Davis, 78 Md. 308

[3] Peatman v. Centerville, etc., Co., 100 Iowa 245, 69 N. W. Rep. 541.

[4] Dudley v. Kentucky High School, 9 Bush (Ky.) 576.

majority of shareholders can regulate and control the lawful exercise of the powers conferred on a corporation by its charter. A holder of shares in an incorporated body, so far as his individual rights and interests may be involved in the doings of the corporation, acting within the legitimate sphere of its corporate power, has no more legal control over them than that which he can exercise by his single vote in the meetings of the company."[1] The court will not interfere with a contemplated contract on the ground that it is improvident and unwise.[2]

The minority stockholders can not maintain an action in their own name for the removal of directors on the ground that three persons who controlled a majority of the stock controlled the election of the seven directors.[3]

§ 433. **Limitation on the power of the majority.**[4]—The right of the majority to control the policy of a corporation is subject to the implication that the business will be managed in the interest of all the stockholders and not merely for that of the majority. If the majority attempt to obtain for themselves an advantage not shared by the other stockholders, a court of equity will interfere at the suit of the minority.[5] In a case where a railway corporation purchased a majority of the stock of a canal company and elected a board of directors in their own interest and appropriated the entire property of the canal company for railway purposes, the railway company was required to pay to the stockholders and creditors of the canal company the difference between the value of the property and what the railway company paid for it.[6] In speaking of the duties of directors the court said: "A director whose personal interests are adverse to those of the corporation has no right to be, or act as, a director."

[1] Durfee v. Old Colony R. Co., 5 Allen (Mass.) 230, Wilgus' Cases; Fluker v. Railway Co., 48 Kan. 577.

[2] Meredith v. New Jersey, etc., Co., 55 N. J. Eq. 211.

[3] Decatur, etc., Co. v. Palm, 113 Ala. 531.

[4] See Wilgus' Cases, Rights of Members Among Themselves and Against the Corporation.

[5] Menier v. Hooper's, etc., Works, 9 L. R. Ch. 350; Sellers v. Phœnix, etc., Co., 13 Fed. Rep. 20; Jones v. Morrison, 31 Minn. 140; Gamble v. Water Co., 123 N. Y. 91.

[6] Goodin v. Cincinnati, etc., Co., 18 Ohio St. 169, on 183.

CHAPTER 16.

TRANSFER OF SHARES.[1]

§ 434. General statement.
435. The right to transfer shares.
436. Power to prohibit transfers.
437. The regulation of transfers.
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440. Transfer on books of the corporation.
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446. Pledge of stock certificates by delivery.
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§ 450. Fraudulent transfer—Rights of transferee or purchaser of stock certificate.
451. Negligence of owner — Estoppel.
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454. Rights of purchaser of shares transferred in violation of a trust.
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456. When the power to sell exists—Presumption of right doing.
457. Lien of corporation upon shares.
458. Effect of a transfer upon rights and liabilities of parties.
459. Remedies for a wrongful refusal to transfer.
460. An action for damages.
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462. Mandamus.

§ 434. **General statement.**—Membership in a private corporation having capital stock may be transferred from one person to another by a transfer of the shares in the manner provided by law. By a complete transfer of shares, the transferee steps into the shoes of the transferrer and thereafter becomes a stockholder in the corporation and is entitled to all the rights and privileges and subject to all the liabilities of membership of which he has, or is presumed to have, notice in such a

[1] See Wilgus' Cases, Rights of Members, Transfer of Shares.

corporation.[1] There must, of course, be authority from both transferrer and transferee for the making of such a transfer. Ordinarily the certificate of shares contains upon its back a written form of assignment and power of attorney authorizing the corporation to make the transfer upon the books of the corporation. The execution of a deed of gift of corporate stock vests the complete beneficial ownership of the shares in the donee and authorizes the corporation upon the presentation of the certificate and deed to make the proper entries on its books.[2] Shares of stock can not be transferred to a person on the books of the corporation so as to make him a stockholder without his consent, but an agreement by a party to take the shares of a stockholder will authorize the transfer of the shares to him.[3]

§ 435. **The right to transfer shares.**—It is implied in the constitution of every private corporation that the shareholders may transfer their shares at will by giving notice of the transfer to the corporation.[4] Like other personal property, shares of stock may be alienated at will unless the general right is restricted by the charter, statute or contract. The right itself is not derived from the charter as has been held,[5] but is an incident of ownership—an incident of the ownership of any species of property, as the unrestricted right of alienation—the *jus disponendi*.[6]

[1] Bank v. Lanier, 11 Wall. 369; Sanger v. Upton, 91 U. S. 56; Scott v. Bank, 15 Fed. Rep. 494.

[2] Thompson v. Hudgins, 116 Ala. 93, and cases therein cited.

[3] Signa, etc., Co. v. Greene, 88 Fed. Rep. 207, 31 C. C. A. 477. In White v. Salisbury, 33 Mo. 150, it was held that a contract to deliver a certain amount in railroad stock was satisfied by a transfer on the book without the delivery of a certificate. See also Boatmen's, etc., Co. v. Able, 48 Mo. 136.

[4] Trisconi v. Winship, 43 La. Ann. 45; Sargent v. Franklin, etc., Co., 8 Pick. (Mass.) 90, 19 Am. Dec. 306; Burrall v. Bushwick R. Co., 75 N. Y. 211; Bank of Attica v. Mfgr. Bank, 20 N. Y. 501; Farmers' Bank v. Wasson, 48 Iowa 336; Jackson v. Newark, etc., Co., 31 N. J. L. 277; Bloede v. Bloede, 84 Md. 129, Wilgus' Cases.

[5] Johnson v. Laflin, 5 Dill. (C. C.) 65.

[6] In re Klaus, 67 Wis. 401; Trisconi v. Winship, 43 La. Ann. 45; Farmers' etc., Bank v. Wasson, 48 Iowa 336; Miller v. Great Republic, etc., Co., 50 Mo. 55; Poole v. Middleton, 29 Beav. 646; Moore v. Bank of Commerce, 52 Mo. 377. The validity of the transfer

§ 436. **Power to prohibit transfers.**—The directors or managing officers of a corporation have no power to prohibit the transfer of shares. Nor is it within the power of the stockholders, unless expressly authorized by the charter, to enact a by-law forbidding the transfer of shares without the consent of the president or board of directors. Where a by-law provided that no valid transfer could be made without the consent of the board of directors, the court said: "Its enforcement would operate as an infringement upon the property rights of others which the law will not permit. It would, besides, operate as a restraint upon the disposition of property in the stock of the corporation, in the nature of restraint of trade, which the courts will not tolerate. As the restriction is not imposed by express authority of the statute of the state, it can not, in such cases, be enforced."[1]

§ 437. **The regulation of transfers.**—Although the corporation can not prohibit the transfer of its shares, it may prescribe reasonable regulations and formalities for the purpose of protecting the corporation.[2] Hence the provisions of a by-law

depends upon the law of the state by which the corporation was created. Black v. Zacharie & Co., 3 How. (U. S.) 482. A pledgee of shares is entitled to have the proper entry for the protection of his rights made on the books of the corporation although his contract is silent on the subject. But he is not entitled to have new certificates issued in his name. Spreckels v. Nevada Bank, 113 Cal. 272, 33 L. R. A. 459. See Miller v. Houston City R. Co., 16 C. C. A. 128, 69 Fed. Rep. 63.

[1] Farmers' Bank v. Wasson, 48 Iowa 336; Wilson v. St. Louis, etc., R. Co., 108 Mo. 588; Sargent v. Franklin, etc. Co., 8 Pick. 90; Quiner v. Marblehead, etc., Co., 10 Mass. 476; Feckheimer v. National Exchange Bank, 79 Va. 80; Barnes v. Brown, 80 N. Y. 527.

[2] Dane v. Young, 61 Maine 160; Planters', etc., Ins. Co. v. Selma, etc., Bank, 63 Ala. 585. As to restrictions upon transfer in by-laws or articles, see Bloede v. Bloede, 84 Md. 129, 33 L. R. A. 107, Wilgus' Cases; Ireland v. Globe, etc., Co. (R. I.), 29 L. R. A. 429. The transfer of membership in such organizations as boards of trade and chambers of commerce are usually subjected to careful restrictions. The decision in State v. Chamber of Commerce (Minn.), 79 N. W. Rep. 1026, seems inconsistent with the correct view of such corporations. The corporation was organized to facilitate the buying and selling of products, to inculcate principles of justice and equity in trade, and to facilitate the speedy adjustment of business disputes among the members. It had no capital stock, but the membership

requiring a transfer on the books of the corporation must be complied with, or there will be no transfer of membership as against the corporation. A grant of power to the directors to regulate transfers does not confer power arbitrarily to restrain transfers at discretion.[1] It merely authorizes the corporation to prescribe formalities to be observed in making transfers. A provision that shares shall be "transferable only on the books of the company" will not authorize the directors to refuse to register a transfer, although they may consider the transfer detrimental to the interest of the corporation.[2] The power to regulate "can only go to the extent of prescribing conditions essential to the protection of the association against fraudulent transfers, or such as may be designed to evade the just responsibilities of the stockholder. It is to be exercised reasonably. Under the pretense of prescribing the manner of the transfer, the association can not clog the transfer with useless restrictions, or make it dependent upon the consent of the directors or other stockholders."[3] The corporation can not without express power determine to whom only transfers may be made.[4] It is sufficient that the transferee is a person who is

was represented by a certificate of stock. The by-laws contained a provision regulating a transfer of membership. Notice of the proposed transfer was to be posted for ten days, and "if no objection shall have been made on account of any unsettled contracts, claims, demands, or complaints against the holder of such membership," it may be transferred upon paying a small fee. If there are objections, their sufficiency shall be determined by the board of directors. A member was adjudged a bankrupt and discharged from his debts. His trustee in bankruptcy sold the certificate, and the purchaser demanded a transfer of the membership to him. Objections were made by members who held claims against the bankrupt which were discharged by the order. The board of directors refused to permit the transfer, but the court held that the debts gave the objectors no standing, and ordered the transfer made. It is settled by the decisions of the federal courts that a debt is not paid by a discharge in bankruptcy. It is simply unenforcible.

[1] Moffatt v. Farquhar, L. R. 7 Ch. Div. 591; Ex parte Penney, L. R. 8 Ch. App. Cas. 446; Robinson v. Bank, L. R. 1 Eq. 32.

[2] Chonteau Spring Co. v. Harris, 20 Mo. 382; Feckheimer v. Nat'l, etc., Bank, 79 Va. 80.

[3] Johnston v. Laflin, 103 U. S. 800.

[4] In Chonteau Spring Co. v. Harris, 20 Mo. 382, it was held that the mere power to regulate transfers does not authorize a refusal to allow a transfer to an insolvent. But see § 568. In Moore v. Bank, 52 Mo. 377, it was held that a by-law prohibiting the

capable of assuming the obligations of a shareholder. The transfer may be by or to an officer or director so long as it is in good faith, and no advantage is taken of the position of the parties.

The motive which induces the purchaser of shares to ask for their transfer is in general immaterial. Where one who represented a rival business corporation, and who had been conducting a series of suits against the Standard Oil Trust, purchased shares in the trust and demanded their transfer, the court said: "The plaintiff purchased the shares of the trust with his own money, and he represents no interests or purposes other than his own in this action. His claim is founded upon a right of property lawfully acquired. * * * When no discretionary power is reserved to that effect, there is not, nor should there be, any rule of law which will enable a corporation or company whose stock is on sale in the open market, to discriminate between bona fide purchasers who invest money in it for their own benefit, or to deny to some of them the right to make their title effectual. * * * In the present case no such discretionary powers seem to have been vested in the trustees. And the purchase of the stock was open to the plaintiff and fairly made by him. Attached to it was the quality of transferability, and with it was presumptively the right of the beneficial holder to have recognition as such by means of transfer to him on the books of the trust. * * * In such case it is difficult to see that motive legitimately becomes a subject of consideration, unless the relief in view may for that reason result unjustly to others in whose behalf it is resisted, or to the prejudice of their legal rights."[1]

§ 438. **Restrictions imposed by by-law or express contract.**— It has been held that a by-law which prohibits a transfer of

alienation of shares or imposing restrictions upon their transfer was against public policy and void as in restraint of trade.

[1] Rice v. Rockefeller, 134 N. Y. 174, Wilgus' Cases, citing Bloxam v. Railway Co., 3 Ch. App. 337; Ramsey v. Gould, 57 Barb. (N. Y.) 398. A by-law providing that a transfer of the stock of an irrigation company shall be made only with the bond for which it was issued does not apply to a sale of delinquent stock for assessments. Spurgeon v. Santa Ana, etc., Co., 120 Cal. 71, 39 L. R. A. 701.

shares to one not already a stockholder without first offering the shares to the corporation is invalid,[1] and that in so far as a by-law prohibiting a transfer without the consent of the board of directors implies an express agreement between the corporation and the stockholders it is void as against public policy.[2] So on agreement by the organizers of a corporation that their stock shall be put in trust and not drawn out for six months without the written consent of all is void as against public policy if it is to be construed so as to prevent a sale of the stock within the six months.[3] But under charter authority the ownership of stock in the corporation may be restricted to a certain class of persons,[4] and in the absence of a charter provision to the contrary the members of a reservoir corporation may lawfully agree that rights in their capital stock shall pass with mill property owned by such members, so that the ownership shall be confined solely to those directly interested in the maintenance of the dams.[5]

It was held in Massachusetts[6] that even if a by-law of a corporation which gives the board of directors the option to take the shares of any stockholder who desires to sell them at a valuation to be determined by them is invalid, the stockholder is bound by an agreement which adopts the by-law. The by-law provided that a member who desired to sell his shares should cause the shares to be appraised by the directors and thereupon offer them to the corporation at such appraised value, and that if the directors, if they think it for the best

[1] Brinkerhoff, etc., Co. v. Home, etc., Co., 118 Mo. 447, Wilgus' Cases.

[2] Feckheimer v. Bank, 79 Va. 80.

[3] Williams v. Montgomery, 68 Hun (N. Y.) 416; Fisher v. Bush, 35 Hun (N. Y.) 641; Nesmith v. Washington Bank, 6 Pick. (Mass.) 324.

[4] Blien v. Rand (Minn.), 79 N. W. Rep. 606.

[5] McGinty v. Athol, etc., Co., 155 Mass. 183, Wilgus' Cases.

[6] New England, etc., Co. v. Abbott, 162 Mass. 148, 27 L. R. A. 271. In Ireland v. Globe, etc., Co., 20 R. I. (Part I) 192, 38 L. R. A. 299, it was held that a corporation could not enforce a contract between proposed incorporators that they will not transfer their stock without giving the option of purchase to the corporation. The remedy, if any, is for breach of contract. In Burden v. Burden (N. Y.), 54 N. E. Rep. 17, an agreement between the promoters which contained a restriction upon the right to transfer the shares was assumed to enter into the charter and be valid.

interests of the company, shall tender such appraised value and that the stockholder shall then make a transfer to the corporation. The certificates contained on their face the statement that "said shares are transferable in person or by attorney, duly constituted, on the books of the company and in the manner and upon the conditions expressed in the by-laws of the company, printed upon the back of this certificate." At the time the certificates were issued the stockholder signed a receipt which stated that he "received the above certificates subject to the conditions and restrictions therein referred to and to the by-laws of the company to which I agree to confirm."

In a suit by the corporation against the executors of the estate of the stockholder for specific performance of the agreement to convey, the court said: "The defendant contends that these by-laws are void. We have not found it necessary to consider that question and we express no opinion upon it. We think that the case may well stand on the ground that the defendant's testator entered into an agreement with the plaintiff to do what the plaintiff now seeks to compel his executor to do. It is manifest that a stockholder may make a contract with a corporation to do or not to do certain things in regard to its stock, or to waive certain rights or to submit to certain restrictions, respecting which the stockholders might have no power of compulsion over him." In Adley v. Whitstable Co.[1] Lord Eldon says: 'It has been frequently determined that what may well be made the subject of a contract between the different interests of a partnership would not be good as a by-law. For instance, an agreement amongthe citizens of London * * * * that they would not sell except in the markets of London would be good; yet it has been declared by the legislature that a by-law to that effect is bad.'[2] In the present case, the certificates were issued to the defendant's testator in consideration of the payment by him to the corpo-

[1] Adley v. Whitstable Co., 17 Ves., Jr., 315, 322.

[2] Davis v. Second Universalist, etc., 8 Met. (Mass.) 321; Bank of Attica v. Bank, 20 N. Y. 501; Cook Stock and Stockholders, § 408.

ration of the amount due for the stock, and the agreements with it on his part, which they contain. By accepting them without objection and by signing the receipts he must be held to have agreed to the conditions printed on the back of the certificates. The fact that the conditions were contained in by-laws which may have been invalid as such does not render his agreement void if the contract was in substance one which the corporation had power to make. We think that it had such power. It is held in this state that a corporation, unless prohibited, may purchase its own stock;[1] and we see nothing opposed to public policy in such an agreement as this with corporations like this. If honestly carried out by the directors, it tends to secure a trustworthy body of stockholders from which those having a share in the management of the corporation naturally would be selected. It certainly can not be contrary to public policy that the managers of this and similar institutions should be persons of skill who possess the confidence of the public. The restraint upon alienation is no greater than is often agreed to. In England it is not unusual to find in the deeds of settlement or articles of association under which corporations or joint stock companies have been organized, and which correspond to the charter and by-laws here, provisions requiring the stockholder, in case he wishes to transfer his stock, to offer it to the directors or to submit to them the name of the transferee for approval.''[2]

The suit being between the company and a stockholder to enforce a contract with the company, and the rights of third parties not being involved, it was held that the plaintiff was entitled to a decree compelling the defendant to convey the shares upon payment by it of the amount of the appraisal, and enjoining him from prosecuting an action at law against the corporation to recover dividends upon the stock.

[1] Dupee v. Boston, etc., Co., 114 Mass. 37.

[2] Bargate v. Shortridge, 5 H. L. Cas. 297; Poole v. Middleton, 29 Beav. 646; Ex parte Penney, L. R. 8 Ch. App. 446; Moffatt v. Farquhar, L. R. 7 Ch. Div. 591; Chappell's Case, L. R. 6 Ch. App. 902.

§ 439. **Regulation of transfers continued.** — Restrictions upon the power to make a bona fide sale and transfer of shares must be based upon authority conferred by the charter, a by-law adopted under the authority of a charter provision,[1] or a valid contract with the stockholder.[2] A by-law which requires the approval and acceptance of a transfer by the board of directors is invalid unless expressly authorized by statute.[3] Charter authority is required for a by-law prohibiting the transfer of shares by a stockholder who is indebted to the corporation.[4] "At common law, and independently of statutory provisions granting or authorizing the exercise of the power, a corporation can not prohibit a transfer of its shares on account of the indebtedness of the shareholder to the corporation. Where the stock is personal property, restrictions upon its transfer must have their source in legislative action, and the corporation itself can not create these impediments."[5] The national banking act gives a stockholder the right to transfer his shares, and this right can not be taken away by a by-law which prohibits a transfer without the consent of the board of directors.[6] This right can not be restricted by a state statute.[7]

§ 440. **Transfer on books of the corporation.**—The requirement that the stock can only be transferred upon the books of the corporation is almost universal. Such provision is generally held to be for the protection and benefit of the corporation and as not preventing a shareholder from transferring his shares without an entry on the books. Except as against the corporation the shareholder may, as an incident of his

[1] Johnson v. Laflin, 5 Dill. 65, 103 U. S. 800.

[2] See New England, etc., Co. v. Abbott, 162 Mass. 148, 27 L. R. A. 271.

[3] Farmers', etc., Bank v. Wasson, 48 Iowa 336, 30 Am. Rep. 398.

[4] Feckheimer v. Bank, 79 Va. 80; Byron v. Carter, 22 La. Ann. 98. But see Spurlock v. Railroad Co., 61 Mo. 319; Mechanics' Bank v. Merchants' Bank, 45 Mo. 513, 100 Am. Dec. 388; Bank of Attica v. Bank, 20 N. Y. 501.

[5] Carroll v. Mullanphy, etc., Bank, 8 Mo. App. 249. See § 457.

[6] Johnson v. Laflin, 5 Dill. 65, 103 U. S. 800; Feckheimer v. Bank, 79 Va. 80; Bank of Attica v. Bank, 20 N. Y. 501.

[7] Doty v. First Nat'l Bank, 3 N. Dak 9, 17 L. R. A. 259.

right of property, transfer both the legal and equitable title to his share.[1] As between the immediate parties to the transaction, a common-law assignment of the shares is effectual and will be recognized and enforced as against all parties not showing a superior right.[2] The "purpose of such a regulation is to afford the corporation and persons dealing with it the means of ascertaining who are its shareholders. Without an entry of a transfer upon its books it would be practically impossible for the corporation to know who are entitled as its shareholders to vote at its meetings, to whom dividends are to be paid, and who are liable as shareholders to the corporation or its creditors. With such an entry the books become a record showing who at any particular time are the shareholders, and who as such are entitled to the rights conferred, and subject to the liabilities imposed by membership in the corporation. A regulation of this kind, then being intended merely to promote the convenient administration of the corporate affairs, is given binding effect upon the corporation no further than is necessary for the accomplishment of that end. Hence it is competent for the corporation, for whose advantage the regulation is made, to insist upon a strict compliance with the formalities prescribed, if not itself in fault, or to waive them if it sees fit."[3]

In New York it was said:[4] "It has been settled by repeated

[1] Baldwin v. Canfield, 26 Minn. 43; Nicollet Nat. Bank v. City Bank, 38 Minn. 85; Joslyn v. St. Paul, etc., Co., 44 Minn. 183; Lund v. Wheaton, etc., Co., 50 Minn. 36, 52 N. W. Rep. 268; Continental Nat. Bank v. Eliot Nat. Bank, 7 Fed. Rep. 369; McNeil v. Tenth Nat. Bank, 46 N. Y. 325, Wilgus' Cases; Grymes v. Hone, 49 N. Y. 17; Turnpike Co. v. Gerhab (Pa.), 13 Atl. Rep. 90; Thurber v. Crump, 86 Ky. 408; Robinson v. National Bank, 95 N. Y. 637; Isham v. Buckingham, 49 N. Y. 216; Mandlebaum v. Mining Co., 4 Mich. 464.

[2] Nicollet Nat. Bank v. City Bank, 38 Minn. 85; Dickinson v. Central Nat. Bank, 129 Mass. 279. That a good equitable title vests in the transferee see Hubbard v. Manhattan Trust Co., 87 Fed. Rep. 51, 57 U. S. App. 730.

[3] American Nat. Bank v. Oriental Mills, 17 R. I. 551, 23 Atl. Rep. 795; Isham v. Buckingham, 49 N. Y. 216; Chemical Nat. Bank. v. Colwell, 132 N. Y. 250.

[4] McNeil v. Bank, 46 N. Y. 325, Wilgus' Cases. An entry on the books of the corporation is not necessary to vest in the vendee all the title which the vendor had. Parker v. Bethel, etc., Co., 96 Tenn. 252, 31 L. R. A. 706. The transferee will get an equi-

adjudications that as between parties the delivery of the certificate, with assignment and power indorsed, passes the entire title, legal and equitable, in the shares, notwithstanding that by the terms of the charter or by-laws of the corporation, the stock is declared to be transferable only on its books, that such provisions are intended solely for the protection of the corporation, and can be waived and asserted at its pleasure, and that no effect is given to them except for the protection of the corporation, that they do not incapacitate the shareholder from parting with his interest, and that his assignment, not on the books, passes the entire legal title to the stock, subject only to such liens or claims as the corporation may have upon it, and excepting the right of voting at elections, etc.''

§ 441. **Transfer on books continued.**—Other decisions are to the effect that the provision requiring a transfer on the books of the corporation is exclusive of any other mode. The legal title is held to remain in the transferrer until the certificate is deposited with the corporation for transfer.[1] In an early case the supreme court ''took notice of the distinction between the legal and equitable title in cases of bank stock where the charter of the bank had provided for the mode of transfer. The general construction, which has been put upon the charters of other banks containing similar provisions as to the transfer of their stock, is that the provisions are designed solely for the safety and security of the bank itself, and of purchasers without notice; and that as between vendor and vendee a transfer not in conformity to such provisions is good to pass the equitable title and divest the vendor of all interest in the stock.''[2]

When it was contended that the provision was merely a

table title which will be protected as against all persons not showing a superior title. Prince, etc., Co. v. St. Paul, etc., Co., 68 Minn. 121.

[1] In Brown v. Adams, 5 Biss. (C. C.) 181, it was held that a mere delivery of the certificate to the officers of the corporation is not sufficient to pass title. See Lippitt v. American, etc., Co., 15 R. I. 141, 2 Am. St. Rep. 886.

[2] Union Bank v. Laird, 2 Wheat. (U. S.) 390; Block v. Zacharie & Co., 3 How. (U. S.) 482; Reed v. Copeland, 50 Conn. 479; Bank v. Gridley, 91 Ill. 457; Leyson v. Davis, 17 Mont. 220, 31 L. R. A. 429.

regulation for the convenience and protection of the bank, Chief Justice Shaw said: "We can see no ground upon which to restrict the plain provision of the statute. If we may judge of an intended operation of an act of legislation from the useful and beneficial purposes it may tend to promote, we should construe it as having a much broader and more comprehensive scope." It was therefore held that a creditor of the stockholder who attached the shares before the transfer on the books acquired title as against the holder of an unrecorded transfer.[1]

Where this rule is adhered to, the holder of shares may make an equitable assignment of his interest without an assignment of his stock on the books of the company, and the interest of the assignee will be protected in equity.[2] As between the transferrer and the transferee the "transfer is complete by the sale, assignment and delivery and payment, without registration, whether the transferee gets the legal title before registration or only a complete equitable title."[3] In any case, the transferee as against the corporation acquires only the right to have the transfer made to him on the books of the corporation. Where the corporation is entitled to a lien on the shares, he takes the title whether legal or equitable subject to claims the corporation may have against the stock.[4] Until the transfer is made the corporation may treat the transferrer as the stockholder; although if it has notice of the rights of the transferee it will not be justified in disregarding him under all circumstances. A transferring stockholder is released from his liabilities as a stockholder by a legal transfer of the shares, and if the corporation wrongfully refuses to make the transfer, it can not thereafter hold the transferrer to the liabilities

[1] Fisher v. Essex Bank, 5 Gray (Mass.) 373, Wilgus' Cases. See § 442, *infra*.

[2] Fitchburgh, etc., Bank v. Torrey, 134 Mass. 239; Lippitt v. American, etc., Co., 15 R. I. 141; Peck v. Providence, etc., Co., 17 R. I. 275, 23 Atl. Rep. 967; Smith v. Nashville, etc., R. Co., 91 Tenn. 221, 18 S. W. Rep. 546.

[3] Johnston v. Laflin, 5 Dill. 65, 103 U. S. 800. A provision that the certificate shall be negotiable only by transfer upon the books of the company with its consent first obtained, will not prevent the vesting of a complete equitable title in the assignee by an absolute and unconditional assignment. Hubbard v. Manhattan, etc., Co., 87 Fed. Rep. 51, 30 C. C. A. 520.

[4] Union Bank v. Laird, 2 Wheat. (U. S.) 390.

of a shareholder.[1] But a different rule might apply as against corporate creditors who become such in reliance upon the books of the corporation. In order to be relieved from this liability a transferring stockholder must at least make earnest effort to have the transfer actually made upon the books of the corporation.[2]

It is the duty of the transferee to have the transfer made on the books of the corporation, and if he neglects to do so the transferrer may compel him to do what is necessary to relieve him from further liability to the corporation or its creditors.[3]

§ 442. **Rights of attaching creditors.**[4]—The authorities are in irreconcilable conflict upon the question of the right to priority as between attaching creditors of the transferrer and the holder of an unrecorded transfer of shares. The conflict results from the different views taken by the courts of the nature and purposes of the requirement of a transfer upon the books of a corporation. Practically all of the leading text-writers take the position that the purchaser at the execution sale under such an attachment gets no title as against those who have acquired equities under an unrecorded transfer of the shares. Thus, Morawetz says[5] that "shares in a corporation are mere contract rights or choses in action, while the certificates are treated as the embodiment of the rights and may be considered as chattels. The assignment of a certificate ought, therefore, to have the same effect, as to creditors of the assignor, as the indorsement and delivery of a bill or note.

A creditor does not, by levying an attachment or execution on property, occupy the position of a bona fide purchaser for value. A creditor is entitled only to step into the place of his debtor in respect to the latter's property and contract rights.

[1] Chouteau, etc., Spring Co. v. Harris, 20 Mo. 382.

[2] See §570. Shellington v. Howland, 53 N. Y. 371; Dane v. Young, 61 Maine 160; Richmond v. Irons, 121 U. S. 27; Johnson v. Underhill, 52 N. Y. 202. But the negligent vendee will be liable to the vendor for what he has had to pay. Whitney v. Butler, 118 U. S. 655. If the vendor does everything that a prudent business man would do to have the transfer made, but fails, he is not liable. See, also, Harpold v. Stobart, 46 Ohio St. 397; Chemical Nat'l Bank v. Colwell, 132 N. Y. 250.

[3] Allen v. South Boston, etc., R. Co., 150 Mass. 200, 15 Am. St. Rep. 185; Kellogg v. Stockwell, 75 Ill. 68.

[4] See Wilgus' Cases.

[5] Morawetz Priv. Corp., § 196.

He is not entitled, upon any principles of justice and common honesty, to pay his debt out of property which does not in truth belong to the debtor. A creditor, therefore, ought not to be allowed to levy on shares after the real substantial and equitable ownership has been transferred to a purchaser for value. It is wholly immaterial for this purpose whether the shares have been transferred on the company's books or not. After the assignment the debtor would retain at most a naked legal claim against the corporation, and this is all that the creditor would be entitled to take."

Cook says[1] that "as a general rule it may be said that a purchaser of a certificate of stock is usually protected as fully without a registry on the corporate books as he would be by a registry, so far as subsequent attachments are concerned."

Pomeroy says[2] that by the great majority of decisions an assignment of shares without a record on the books of the corporation "is valid as against creditors of the assignor and gives the assignee a precedence over their subsequent judgments, executions and attachments." This rule is unquestionably settled by the weight of authority, although, as pointed out by a writer in the American Law Review,[3] possibly not by the number of decisions. It is difficult to see why the attaching creditor should acquire a greater interest in the shares than his debtor had at the time of the attachment. The debtor transferrer having parted with his interest in the property and retaining only the bare legal title, the creditor should be permitted to acquire nothing greater. The attachment or execution creditor has no prior equities and can acquire no existing equities by virtue of his levy. He parts with no interest or right and is in no worse condition by the failure of the levy than he was before. If the debtor has no title, the creditor can acquire none by a levy, and there seem to be no reasons in public policy for creating equities where none exist in fact. Therefore a sale, transfer or pledge of corporate stock, although not entered upon the books of the corporation, should be held effectual as between the parties,

[1] Cook Priv. Corp., § 381.

[2] Pomeroy Eq. Jur., § 700.

[3] Mr. I. H. Hatfield, in 30 Am. Law Rev., p. 223, where the authorities are collected and the arguments in favor of creditor strongly stated.

and take precedence of a subsequent levy thereon in behalf of the vendor's creditors.[1] An unrecorded transfer of national bank stock will take precedence of a subsequent attachment on behalf of a creditor without notice.[2]

[1] Lund v. Wheaton, etc., Co., 50 Minn. 36; Baldwin v. Canfield, 26 Minn. 43; Joslyn v. St. Paul, etc., Co., 44 Minn. 183; Doty v. First Nat'l Bank, 3 N. Dak. 9, 17 L. R. A. 259; Robinson v. Bank, 95 N. Y. 637; McNiel v. Tenth Nat'l Bank, 46 N. Y. 325, Wilgus' Cases; New York, etc., R. Co. v. Schuyler, 34 N.Y. 30; Leitch v. Wells, 48 N. Y. 585; Cutting v. Demerel, 88 N. Y. 410; Grymes v. Cone, 49 N. Y. 17; Bank of Utica v. Smalley, 2 Cowen (N. Y.) 770; Smith v. American, etc., Co., 7 Lansing 317; Commercial Bank v. Kortright, 22 Wend. (N. Y.) 348; Stebbins v. Phœnix, etc., Co., 3 Paige (N. Y.) 350; Thurber v. Crump, 86 Ky. 408; Clark v. German, etc., Bank, 61 Miss. 611; Broadway Bank v. McElrath, 13 N. J. Eq. 24; Rogers v. Stevens, 4 Halst. Ch. (N. J.) 167; Mt. Holly, etc., Co. v. Ferree, 17 N. J. Eq. 117; Smith v. Crescent, etc., Co., 30 La An. 1378; Crescent City v. Deblieux, 40 La. An. 155; George R. Barse, etc., Co. v. Range, etc., Co., 16 Utah 59; Finney's App., 59 Pa. St. 398; Eby v. Guest, 94 Pa. St. 160; Seeligson & Co. v. Brown, 61 Tex. 114; May v. Cleland (Mich.), 44 L. R. A. 163; Mandelbaum v. North American, etc., Co., 4 Mich. 464; Newberry v. Detroit, etc., Co., 17 Mich. 140; Nat'l Bank v. Port Townsend, etc., Co., 6 Wash. 597; First Nat'l Bank v. Dickson (Colo. App.), 36 Pac. Rep. 618. The rights of a pledgee of stock are superior to that of a purchaser on execution against the pledgor. Dearborn v. Washington, etc., Bank, 18 Wash. 8. See, also, Morehead v. Western, etc., R. Co., 96 N. C. 362; Lippitt v. American, etc., Co., 15 R. I. 141, 23 Atl. Rep. 111; Colbert v. Sutton, 5 Del. Ch. 294; Noble v. Turner, 69 Md. 519, 16 Atl. Rep. 124; Merchants' Nat'l Bank v. Richards, 6 Mo. App. 454, 74 Mo. 77; White v. Salisbury, 33 Mo. 150. The following cases sustain the rights of the attaching creditor: Masury v. Arkansas Nat'l Bank, 87 Fed. Rep. 381; Ft. Madison, etc., Co. v. Batavian Bank, 71 Iowa 270, 32 N. W. Rep. 336, 60 Am. Rep. 789; Ottumwa Screen Co. v. Stodghill, 103 Iowa 437; Peoples' Bank v. Gridley, 91 Ill. 457; State v. First Nat'l Bank, 89 Ind. 302; Topeka, etc., Co. v. Hale, 39 Kan. 23; Skowhegan Bank v. Cutler, 49 Maine 315, 52 Maine 509; Conway v. John, 14 Colo. 30; Supply, etc., Co. v. Elliott, 10 Colo. 327, 15 Pac. Rep. 691, 3 Am. St. Rep. 586; Marlborough, etc., Co. v. Smith, 2 Conn. 579; Colt v. Ives, 31 Conn. 25; State v. Commissioners, 21 Fla. 1; Fisher v. Essex Bank, 5 Gray (Mass.) 373; Boyd v. Rockport Mills, 7 Gray 406; Dickinson v. Central Bank, 129 Mass. 279; Central Nat'l Bank v. Williston, 138 Mass. 244; Fisher, etc., Co. v. Jones, 82 Ala. 117; Barstow v. Savage, M. Co., 64 Cal. 388; Pinkerton v. Manchester, etc., R. Co., 42 N. H. 424; Scripture v. Soapstone Co., 50 N. H. 571–585; Buttrick v. Nashua, etc., R. Co., 62 N. H. 413, 13 Am. St. Rep. 578; Cheever v. Myer, 52 Vt. 66; In re Murphy, 51 Wis. 519.

[2] Doty v. First Nat'l Bank, 3 N. Dak. 9, 17 L. R. A. 259; Sibley v. Quinsigamond Nat'l Bank, 133 Mass. 515; First Nat'l Bank v. Lanier, 11 Wall. (U. S.) 369; Continental Bank v. Bank, 7 Fed. Rep. 369; Hazard v. Bank, 26 Fed. Rep. 94.

It is sometimes provided by statute that no transfer of shares shall be valid as against creditors unless a record of the transfer is made in some public office. Under such a statute an attachment takes precedence over an unrecorded transfer.[1] Under the Iowa statute, which provides that a transfer of shares is not valid except as between the parties thereto until it is regularly entered upon the books of the company, an attaching creditor secures the stock, although he had knowledge of the unrecorded transfer.[2] Where there is no requirement of transfer on the books of the corporation a common-law assignment by delivery of the certificate with a written transfer conveys a good title to the shares as against an attaching creditor.[3]

§ 443. **Transfers in fraud of creditors.**—A transfer of the shares upon the books of the corporation may be necessary in order to avoid the effect of a statute which renders the sale of personal property presumptively fraudulent where there is not a complete delivery of the property, as against the creditors of the vendor. In some jurisdictions the presumption is conclusive, while in others it may be overcome by evidence. Upon this general principle the attaching creditor of the transferrer is sometimes able to prevail over the holder of a certificate which has not been transferred upon the books of the corporation. In Connecticut it was said:[4] "The ground on which stock sold, but not legally transferred, is open to attachment by the creditors of the vendor, is the same upon which personal chattels sold but retained in the possession of the vendor are liable to attachment by the vendor's

[1] Masury v. Arkansas Nat'l Bank, 87 Fed. Rep. 381, citing Berney Nat'l Bank v. Pinckard, etc., Co., 87 Ala. 577; Murphy's App., 51 Wis. 519; Ft. Madison, etc., Co. v. Batavian Bank, 71 Iowa 270, 60 Am. Rep. 789; Newell v. Williston, 138 Mass. 240.

[2] Ottumwa Screen Co. v. Stodghill, 103 Iowa 437, citing First Nat'l Bank v. Hastings, 7 Colo. App. 129; Lyndonville Nat'l Bank v. Folsom, 7 N. M. 611. *Contra*, George R. Barse, etc., Co. v. Range, etc., Co., 16 Utah 59.

[3] Boston, etc., Assn. v. Cory, 129 Mass. 435.

[4] Colt v. Ives, 31 Conn. 25. See Hotchkiss, etc., Co. v. Union Nat'l Bank, 37 U. S. App. 86. Under such a view of the law, it is necessary that the transfer on the record should be made within a reasonable time. See Pinkerton v. Railway Co., 42 N. H. 424.

creditors. The principle in each case is that the retention of possession by the vendor is a badge of fraud; that is, is evidence of a fraudulent secret trust.''

§ 444. **Manner of making assignment and transfer.**—Where no manner of transfer is prescribed by the charter or by-law it may be made by a delivery of the certificate with the written assignment thereon.[1] At common law this would transfer both the legal and the equitable title and was good as against the corporation and all other persons. It required a clear provision of the charter itself or of some statute to take from the owner of such property the right to transfer it in accordance with the known rules of the common law. By these rules, the delivery of a stock certificate with a written transfer of the same to a bona fide purchaser is a sufficient delivery to transfer the title as against a creditor of the transferer.[2] This common-law right can not be restricted without authority, and the corporation can not, in the absence therefor, require transfers to be made only on the books of the corporation.[3] The issue of a new certificate is not necessary to complete a transfer,[4] and the record of the transfer is unnecessary unless required by the charter or by-laws.[5] A valid gift of non-negotiable securities may be made by their delivery to the donee without assignment or indorsement in writing, and a delivery of certificates of stock coupled with words of absolute and present gift vests an equitable title to the stock which is valid as against the donor or a volunteer.[6] Where the transfer is required to be made on the books of the corporation the facts are to be appropriately recorded in some suitable register or stock book, or in some manner formally entered upon the

[1] Scott v. Bank, 21 Blatch. 203, 15 Fed. Rep. 494.

[2] Boston, etc., Assn. v. Cory, 129 Mass. 435; McNeil v. Tenth Nat'l Bank, 46 N. Y. 325.

[3] Sargent v. Railway Co., 9 Pick. (Mass.) 202; Driscoll v. Manufacturing Co., 59 N. Y. 96.

[4] Sayles v. Bates, 15 R. I. 342.

[5] Boatman's, etc., Co. v. Able, 48 Mo. 136; Chouteau, etc., Co., v. Harris, 20 Mo. 382.

[6] Commonwealth v. Crompton, 137 Pa. St. 138. But see Matthews v. Hoagland, 48 N. J. Eq. 455. An assignment of shares not accompanied by a delivery of the certificate is not effective as against a receiver of the debtor. Atkinson v. Foster, 134 Ill. 472.

books. For this purpose the account in a stock ledger showing the names of the stockholders, the number and amount of shares belonging to each, and the source of their titles, whether by original subscription and payment or by transfer from others, meets the requirements of the law.[1] Where the shares were pledged to a bank as collateral security for a debt by a delivery of the stock certificate indorsed to the bank, and nothing was done for a month, when the certificates were delivered to a transfer agent in Boston and new ones received, and notice given by the next mail to the office of the corporation in New Hampshire, it was held that the transfer was not good as against an attachment levied in the latter state before the issue of the new certificates, as there was a want of proper diligence in perfecting the delivery of the stock. "Nor could the exchange of certificates at the transfer agency be regarded as equivalent to record, or the entry for that purpose in the office at Manchester. If forwarded by the transfer agent and recorded, it then would be perfected; but we are unable to regard the act of the transfer agent in respect to the record as anything more than the act of a mere agent of the bank. To give to the notice and entry at the transfer agency the effect of a record, or entry upon the stock books of the corporation, would, as we think, be contrary to the policy of the law, which requires as the chief evidence of ownership the record or entry upon the books of the corporation kept in this state."[2]

A note by the secretary of the corporation on the margin of the stubs of certain certificates of stock transferred as collateral security by the owner, that the transferee holds them as security for a loan, does not constitute a transfer on the books of the corporation as against the creditors of the transferrer, when such transfer was not authorized by either party.[3]

§ 445. **Transfer after insolvency or dissolution.**—"After a corporation has become insolvent it is the duty of the com-

[1] National Bank v. Watsontown Bank, 105 U. S. 217.

[2] Pinkerton v. Railroad Co., 42 N. H. 424.

[3] McFall v. Buckeye, etc., Assn. (Cal.), 55 Pac. Rep. 253. As to sufficient transfer see Basting v. Northern, etc., Co., 61 Minn. 307.

pany to wind up its affairs, call in the outstanding capital, and satisfy the creditors. The shares have ceased to be the subject-matter of legitimate traffic. They are a burden to the owner and a transfer will be merely a subterfuge to avoid liability.'"[1] This is the rule in the United States,[2] but in England a shareholder may transfer his shares to an insolvent for a nominal consideration and for the sole purpose of escaping liability.[3] Upon the dissolution of a corporation the right of a holder to transfer shares necessarily ceases, although a court of equity will recognize a sale of the shareholder's equitable claim.[4]

§ 446. **Pledge of stock certificates by delivery.**—The pledge of a stock certificate by mere delivery without a transfer properly signed vests in the pledgee an equitable title only. In case of default in the conditions of the pledge the pledgee can not enforce his security by the ordinary method of sale, but by going into a court of equity he may obtain the relief necessary to enable him to render his security available.[5] But "a pledge of certificates of stock by mere delivery, or an equitable mortgage thereof, is subject to the equities of third persons and *cestuis que trust*, although he may have a written agreement from the pledgor to execute a legal transfer of the shares. The rule thus limiting the rights of a pledgee by delivery was

[1] Morawetz Priv. Corp. I, § 166.

[2] Everhart v. West Chester, etc., R. Co., 28 Pa. St. 339; Chouteau, etc., Co. v. Harris, 20 Mo. 382; Marcy v. Clark, 17 Mass. 330; Rider v. Morrison, 54 Md. 429. "When shares are not fully paid up and the corporation is in failing circumstances, it is the general rule throughout the United States, that the holder can not validly transfer them to an irresponsible person for the purpose of avoiding further liability in regard to them. The right of transfer can not be exercised in defraud of creditors of the corporation." Taylor, § 749, citing Dauchy v. Brown, 24 Vt. 197; Nathan v. Whitlock, 9 Paige (N. Y.) 152; Gaff v. Flesher, 33 Ohio St. 107.

[3] De Pass's Case, 4 De G. & J. 544; Jessopp's Case, 2 De G. & J. 638.

[4] James v. Woodruff, 2 Denio 574; Waite Insolvent Corp., § 385.

[5] Nesbit v. Macon, etc., Co., 12 Fed. Rep. 686; Johnson v. Dexter, 2 MacArthur 530; Newton v. Fay, 10 Allen (Mass.) 505; Wilson v. Little, 2 N. Y. 443; Colbrooke Col. Sec. (2d ed.), § 276.

enforced in a case where the act of a pledge of the stock was a fraudulent misappropriation.'"[1]

§ 447. **Surrender of old certificate—Fraudulent reissue.**—A corporation should not permit a transfer or issue a new certificate until the old certificate is surrendered, as it is charged with notice of the equities of the holder of the outstanding certificate. The transferee who receives new certificates without requiring a surrender of the old ones is not a bona fide transferee, and can not hold the corporation liable.[2] One who never receives the certificates, but who nevertheless obtains a registry on the corporate books and receives new certificates without a surrender of the old ones, is not liable in damages to a holder of the old certificates, unless he obtained the registry with knowledge that the old certificates had been transferred.[3] If the corporation issues a new certificate it may become liable upon both the outstanding certificates to innocent purchasers for value.[4] The purchaser assumes the duty to see that the vendor of shares surrenders the old certificate and transfers it on the books. It is also the duty of the corporation to see that this is done before it issues a new certificate.[5] The purchaser of a certificate reciting that it is "transferable only

[1] Colbrooke Col. Sec., § 277; Shropshire Unions R. Co. v. Queen, L. R. 7 E. & I. Apps. 496.

[2] Moores v. Citizens' Nat'l Bank, 111 U. S. 156.

[3] Baker v. Wasson, 53 Tex. 150; Scripture v. Francestown, etc., Co., 50 N. H. 571. In Houston R. Co. v. Van Alstyne, 56 Tex. 439, it is held that a corporation is not bound to recognize a person as a stockholder who obtained a registry without a surrender of the old certificate, when a regular registry with a surrender of the certificates had already been made.

[4] Factors', etc., Co v. Marine, etc., Co., 31 La. Ann. 149; Bank v. Lanier, 11 Wall. 369; Bridgeport Bank v. New York, etc., R. Co., 30 Conn. 231; Guilford v. Western, etc., Tel. Co., 43 Minn. 434; Holbrook v. New Jersey, etc., Co., 57 N. Y. 616. The failure to require the production of the old certificate does not, of course, effect the rights of the person to whom a transfer is made upon the books of the corporation. Boatmen's, etc., Co. v. Abel, 48 Mo. 136. "Any act suffered by the corporation that invested a third party with the ownership of the shares, without due protection and surrender of the certificate, rendered it liable to the owner; and it was its duty to resist any transfer in the books without such production and surrender." Cushman v. Thayer, etc., Co., 76 N. Y. 365. But see Guilford v. Western Union, etc., Co., 59 Minn. 332, 61 N. W. Rep. 324.

[5] Allen v. South Boston R. Co., 150 Mass. 200, 15 Am. St. Rep. 185.

on the books of the company, on the indorsement and surrender of this certificate," has a right to rely upon the certificate securing to him the shares which it represents, and he will be fully protected. Until the outstanding certificate is surrendered the corporation can not be compelled to issue a new certificate.[1]

The doctrine of *lis pendens* has no application to a sale and transfer of shares of stock.[2]

If the surrendered certificate, instead of being canceled, is fraudulently transferred by the officers charged with the duty of issuing shares, the corporation would be liable to the innocent purchaser of the same, but it was recently held in New York that there was no liability where the certificates were taken from the safe of the company and fraudulently pledged by the general manager of the corporation. After stating the rule with reference to negotiable instruments and other choses in action, Chief Justice Andrews said: "Nor, in our opinion, can the judgment below be sustained upon any principle of agency in Jurgens, express or implied, to issue the surrendered certificates, which on the issue of the new certificates become mere vouchers in the possession of the company. If it can be said that the direction of the president to Jurgens to cancel the certificates made him the agent of the company for that purpose, it was an authority to destroy and not to use. His act in abstracting them from the safe and uttering them as valid certificates had no relation to the authority conferred. It was not an act of the same kind as that he was authorized to perform. He had no apparent authority to issue them as genuine certificates, because he had no authority to issue certificates for any purpose. * * * The certificates were at all times after their surrender, and before they were abstracted by Jurgens from the safe of the defendant, in the legal possession of the company. The company never placed them in

[1] Joslyn v. St. Paul, etc., Co., 44 Minn. 183; Lund v. Wheaton, etc., Co., 50 Minn. 36, 52 N. W. Rep. 268. In case of lost certificates, see Guilford v. Western Union, etc., Co., 59 Minn. 332, 61 N. W. Rep. 324.

[2] Holbrook v. New Jersey, etc., Co., 57 N. Y. 616; Bean v. Trust Co., 122 N. Y. 622; but see Sprague v. Manufacturing Co., Fed. Cas. B. 249, 10 Blatchford 173. See an article in 19 Nat. Corp. Rep. 116, and Burford v. Keokuk, etc., Co., 3 Mo. App. 159.

the possession of Jurgens or invested him with the *indicia* of ownership. He had access to the safe as the mere servant of the defendant. The doctrine of implied agency is, we think, wholly inapplicable to the circumstances of the case."[1]

§ 448. **Evidence of transferee's right.**—The officers of the company are the custodians of its stock books, and it is their duty to see that all transfers of shares are properly made, either by the stockholders themselves or persons having authority from them.[2] If upon the presentation of a certificate for transfer, they are at all doubtful of the identity of the party offering it with its owner, or if not satisfied of the genuineness of a power of attorney produced, they can require the identity of the party in the one case and the genuineness of the document in the other to be satisfactorily established before allowing the transfer to be made.[3]

A transfer from the owner to his agent is not authorized by the fact that the principal has given his agent a general power of attorney "to sell, dispose of, transfer and deliver all or any of my interest in the capital stock of any association, bodies corporate or politic." In such a case the corporation was held liable when it accepted the surrender of the certificate not indorsed by either the owner or agent and issued a new certificate in the name of the agent.[4] But the corporation is not bound to assume and act on the theory that a transferrer is attempting a fraud.[5]

§ 449. **Indorsement of certificate.**—The execution of an assignment in blank with power of transfer, upon the back of a certificate of stock, is a warranty of the genuineness of the paper, which may be enforced by any bona fide purchaser of the certificate who fills up the assignment with his name.[6] But

[1] Knox v. Eden Musee, etc., Co., 148 N. Y. 441, 31 L. R. A. 779.

[2] Corporations must see that no unauthorized transfers are made and are liable to any one injured by a breach of this duty. Marbury v. Ehlen, 20 Am. St. Rep. 467.

[3] Chief Justice Waite in Telegraph Co. v. Davenport, 97 U. S. 369; Thompson v. Stanley, 25 N. Y. Supp. 890; Peck v. Bank of America, 16 R. I. 710.

[4] Tafft v. Presidio, etc., R. Co., 84 Cal. 131, 18 Am. St. Rep. 166.

[5] Hughes v. Drovers, etc., Bank, 86 Md. 418.

[6] Matthews v. Massachusetts Nat'l Bank, 1 Holmes 396.

it is not a warranty that the certificate represents valid shares.[1]

§ 450. **Fraudulent transfer[2]—Rights of transferee or purchaser of stock certificate.**—Stock certificates are not negotiable instruments, and hence as a general rule the purchaser of such choses in action can acquire no better title than his vendor has to convey. The true owner of certificates which are stolen and wrongfully transferred can not be deprived of his property, although he may be of the certificates, unless he has been guilty of some negligence or has placed himself in a position where he is estopped to assert his claim. A person can only be deprived of his property by his own consent or through his own negligence. A bona fide purchaser of a negotiable bill, bond or note, although he buys from a thief, acquires a good title if he pays value for it without knowledge of the infirmity of his vendor's title. But as a certificate of stock is not negotiable paper, and the purchaser of such a certificate, although it is indorsed in blank by the owner, obtains no better title to the stock than his vendor had in the absence of all negligence of the part of the owner.[3] "Neither the absence of blame on the part of the officers of the company in allowing an unauthorized transfer of stock nor the good faith of the purchaser of stolen property will avail as an answer to the demand of the true owner."[4] Hence, a bona fide purchaser of stock standing on the company's books in the name of the former owner, regularly indorsed by him, and stolen from the owner, gets no title to the stock.[5] But as against the corporation the purchaser of a certificate of stock in the open market, without knowledge of fraud in its issue by the corporation or its agent, is entitled to have it transferred to him on the books

[1] Peoples Bank v. Kurtz, 99 Pa. St. 344.

[2] See Wilgus' Cases.

[3] Mechanics' Bank v. N. Y., etc., R. Co., 13 N. Y. 599.

[4] Telegraph Co. v. Davenport, 97 U. S. 369; Knox v. Eden, etc., Co., 148 N. Y. 441, 31 L. R. A. 779.

[5] Barstow v. Savage, etc., Co., 64 Cal. 388, 49 Am. Rep. 705; East Birmingham, etc., Co. v. Dennis, 85 Ala. 565, Wilgus' Cases; Machinists Nat'l Bank v. Field, 126 Mass. 345; Shaw v. Spencer, 100 Mass. 382; Hall v. Road Co., 70 Ill. 673. See §§ 323, 324, *supra*.

of the company without reference to any fraud or irregularity in its issue.[1] It will be observed that it is the purchaser of the stolen certificates who can acquire no rights as against the true owner. If through any means the certificate is returned to the corporation and by it taken up and a new certificate issued, new rights are thereby created, and subsequent innocent transferees of the new certificate are protected in their right against the corporation, while at the same time the original owner of the stock may also require the corporation to protect him in his rights as a stockholder, or respond in damages.[2] The courts have been frequently urged to extend the qualities of negotiability to stock certificates and to clothe them with the qualities of commercial paper, so as to make a transfer in good faith for value equivalent to actual title, although there was no agency in the transferrer, and the certificate has been lost without the fault of the true owner, or has been obtained by theft or robbery. But they have refused to adopt this view and there are no cases entitled to be regarded as authority which deny to the owner of a stock certificate which has been stolen or lost without his negligence, the right to reclaim it from the hands of any person in whose possession it subsequently comes, although the holder may have taken it in good faith and for value.

§ 451. **Negligence of owner—Estoppel.**—While the owner of shares of stock can not be deprived of his property by wrongful acts of others, he may by his acts place himself in a position where he will not be permitted to assert his rights as against one who in the eye of the law is entitled to greater

[1] Cincinnati, etc., R. Co. v. Citizens' Nat'l Bank, 56 Ohio St. 351. "One in possession of a certificate of stock of an incorporated company, accompanied by an assignment in blank, executed by the record owner, with an irrevocable power of attorney, authorizing the transfer of the stock, is presumptively the equitable owner of the shares, whose title thereto can not be impeached if he has given value for them without notice of any intervening equity." Matthews v. Hoagland, 48 N. J. Eq. 455.

[2] As to liability of the corporation on fraudulent certificates issued by its officers to innocent persons see § 323. Tome v. Railway Co., 39 Md. 36, 17 Am. Rep. 510; Allen v. Railway Co., 150 Mass. 200; Fifth Ave. Bank v. 42d St., etc., R. Co., 137 N. Y. 231; Knox v. Eden Musee, etc., Co., 148 N. Y. 441.

consideration. Thus, where the holder of a stock certificate indorsed in blank is clothed with power as the agent or trustee, and makes a transfer in excess of his power or in violation of his trust, the true owner is estopped to assert his title as against a third person who, acting in good faith, takes a transfer of the certificate for value from the apparent owner.[1] Such cases rest upon the principle that it is more just and reasonable, where one of two innocent parties must suffer loss, that he should be the loser who has put trust and confidence in the deceiver than the stranger who has been negligent in trusting no one.[2] The possession of a certificate confers an apparent right to the ownership of the shares. The holder possesses "all the external indicia of the title to the stock, and the apparently unlimited power of disposition over it. He does not appear to have, as is said in some of the authorities cited concerning the assignees of choses in action, a mere equitable interest which is said to be notice to all persons dealing with him that they take subject to all equities, latent or otherwise, of third parties; but apparently the legal title and the means of transferring such title in the most effectual manner."[3] The purchaser of a certificate in good faith has a right to rely upon the fact that it will secure to him the shares of stock which it purports to represent.[4] The fact of negligence will, of course, depend upon the circumstances of each case.

[1] McNeil v. Tenth Nat'l Bank, 46 N. Y. 325, Wilgus' Cases; Merchants' Nat'l Bank v. Livingston, 74 N. Y. 223, Wilgus' Cases; National, etc., Co. v. Gray, 12 App. Cas. (D. C.) 276; New York, etc., R. Co. v. Schuyler, 34 N. Y. 30; Mt. Holly, etc., Co. v. Ferree, 17 N. J. Eq. 117; Winter v. Montgomery, etc., Co., 89 Ala. 544, Wilgus' Cases; Otis v. Gardner, 105 Ill. 436; Walker v. Railway Co., 47 Mich. 338; Burton's App., 93 Pa. St. 214; Prall v. Tilt, 28 N. J. Eq. 479.

[2] "For, seeing that somebody must be the loser by this deceit, it is more reasonable that he that employs and puts a trust and confidence in the deceiver should be the loser than a stranger." Lord Holt in Hern v. Nichols, 1 Salk, 289. "Whenever one of two innocent persons must suffer by the act of a third, he who has enabled the former to occasion the loss must sustain it." Ashurst, J., in Lickbarrow v. Mason, 2 D. & E. 70.

[3] Rapallo, J., in McNeil v. Tenth Nat'l Bank, 46 N. Y. 325, Wilgus' Cases.

[4] Joslyn v. St. Paul, etc., Co., 44 Minn. 183; Bridgeport Bank v. New York, etc., R. Co., 30 Conn. 231.

§ 452. **Transfer on forged power of attorney—Liability of corporation.**—If the corporation transfers the shares of one of its members on its books in recognition of a forged power of attorney indorsed upon the certificate, it incurs an alternative liability, either (*a*) to the original shareholder who is free from fault, for a conversion of his shares,[1] or (*b*) to a bona fide sub-transferee of the shares who has purchased them on the faith of the new certificate which the corporation has been induced to issue in consequence of the forgery.[2] The rule is the same as in the case of an unauthorized issue of shares by the corporation without authority. The innocent holder of the certificate can not be ordered "to return his certificate because he purchased the shares in good faith and for a valuable consideration, and the certificate issued to him is as against the bank conclusive evidence of his title. The bank has no right to compel him rather than any other stockholder to give up his certificate and thereby assume the responsibility of its own illegal act."[3] There is no liability to the first transferee of the certificate,[4] nor to one who took the new certificate with notice of the forgery, or of facts sufficient to put him on inquiry.[5] But the corporation may maintain an action against him on his warranty of the genuineness of the power of attorney.[6]

The question of the negligence of the corporation is imma-

[1] Western U. Tel. Co. v. Davenport, 97 U. S. 369; Tafft v. Railroad Co., 84 Cal. 131. See East Birmingham Land Co. v. Dennis, 85 Ala. 565, Wilgus' Cases. The corporation may be compelled to issue new certificates in lieu of those cancelled although the assignees were innocent purchasers. Chicago, etc., Co. v. Fay, 164 Ill. 323. See Pennsylvania Co. v. Franklin, etc., Co., 181 Pa. St. 40; Sewall v. Boston, etc., Co., 4 Allen 277; Davis v. Bank of England, 2 Bing. 393.

[2] Mandlebaum v. Mining Co., 4 Mich. 465; Machinists' Nat'l Bank v. Field, 126 Mass. 345; New York, etc., R. Co. v. Schuyler, 34 N. Y. 30.

[3] Machinists' Nat'l Bank v. Field, 126 Mass. 345.

[4] Simm v. Anglo-Amer. Tel. Co., 5 L. R. Q. B. Div. 188.

[5] Moores v. Bank, 111 U. S. 156.

[6] Boston, etc., R. Co., v. Richardson, 135 Mass. 473. The subject of the transfer of shares on forged powers of attorney is elaborately discussed by Judge Thompson in 26 Am. L. Rev. 809. See also Balkis, etc., Co. v. Tomkinson, L. R. (1893) A. C. 396. As to the liability of one who indorses a forged certificate in blank to subsequent good faith purchaser see Matthews v. Mass. Nat'l Bank, 1 Holmes 396.

terial, as it is liable, although entirely free from negligence. It must take the responsibility of the transfer being genuine, and may refuse to recognize the same until satisfied of its genuineness.[1] Under the English authorities the person to whom the corporation issues a new certificate becomes a member of the corporation, and the former stockholder who was deprived of his shares by forgery is entitled to recover from the company the value of the shares at the time he was deprived of them.[2]

§ 453. **Forgery of transfer—Negligence.**—In a leading case[3] it appeared that the guardian of the owners of certain shares of stock placed the certificates in a box and deposited them in the vault of the bank for safe keeping. The certificates were in the name of the owners, and contained on the back a blank form of transfer and power of attorney. One of the officers of the bank, a brother of the guardian, had access to the box for the purpose of detaching the coupons from certain bonds which were also kept there, and collecting the interest thereon as it became due. He took the certificates, forged the names of the owner to the transfer and power of attorney and sold them to an innocent purchaser for value, who had them transferred on the books of the corporation by means of the forged power of attorney. In a suit against the corporation to compel it to replace the shares, Mr. Justice Field said: "Upon the facts stated there ought to be no question as to the right of the plaintiffs to have their shares replaced on the books of the company and proper certificates issued to them and to recover the dividends accrued on the shares after the unauthorized transfer; or to have alternative judgments for the value of the shares and the dividends. Forgery can confer no power nor transfer any rights. The officers of the company are the custodians of its stock books, and it is their duty to see that all transfers of

[1] Chew v. Bank, 14 Md. 299.

[2] In re Bahia, etc., R. Co., L. R. 3 Q. B. 584. That the wronged stockholder is entitled to have his name placed back on the books of the corporation see Kisterbock's App., 127 Pa. St. 601; Keller v. Eureka, etc., Co., 43 Mo. App. 84.

[3] Telegraph Co. v. Davenport, 97 U. S. 369.

shares are properly made, either by the stockholders themselves or persons having authority from them. If upon the presentation of a certificate for transfer they are at all doubtful of the identity of the party offering it with its owner, or if not satisfied of the genuineness of a power of attorney produced, they can require the identity of the party in the one case and the genuineness of the document in the other to be satisfactorily established before allowing the transfer to be made. In either case they must act upon their own responsibility. In many instances they may be misled without any fault of their own just as the most careful person may sometimes be induced to purchase property from one who has no title, and who may perhaps have acquired its possession by force or larceny. Neither the absence of blame on the part of officers of the company in allowing an unauthorized transfer of stock nor the good faith of the purchaser of stolen property will avail as an answer to the demand of the true owner. The great principle that no one can be deprived of his property without his consent except by the processes of the law requires, in the cases mentioned, that the property wrongfully transferred or stolen should be restored to its rightful owner. The maintenance of that principle is essential to the peace and safety of society, and the insecurity which would follow any departure from it would cause far greater injury than any which can fall in cases of unlawful appropriation of property upon those who have been misled and defrauded."

It was further held that there was no such negligence as would preclude the owner of the shares from asserting her right as against the bank.

§ 454. **Rights of purchasers of shares transferred in violation of a trust.**—Where the legal title and apparently unrestricted power of disposition are vested in a person, the purchaser from him for a valuable consideration, without notice of a secret trust upon which the shares are held, is unaffected by the trust. In such a case the equities of the purchaser are equal to those of the defrauded beneficiary, and the purchaser having also the legal title will prevail. Thus, a purchaser

from one who lawfully has the certificate of stock upon which there is a power of attorney properly signed by the last registered owner apparently authorizing their absolute transfer to any person, takes the stock free from any secret trust existing back of the registry.[1] But a pledge by a trustee of stock confers no right upon one who takes with actual or constructive knowledge of the trust. As said by the New York Court of Appeals,[2] "Any person who receives property knowing that it is the subject of a trust, and that it has been transferred in violation of the duty or power of the trustee, takes it subject to the right not only of the *cestui que trust*, but also of the trustee to reclaim possession of the property. Knowledge of the trustee's violation of the trust condition will be chargeable to the person dealing with him, if the facts were such as in reason to put him upon inquiry, and to require him to make some investigation, as the result of which the true title and authority of the trustee might have been disclosed. He will then be regarded as having constructive notice of the terms of the trust whence the trustee derives his power to act." One who purchases from an executor is chargeable with notice of the contents of the will which is on record.[3] A sale by an executor in violation of a statute passes no title to the purchaser, and where an administrator can transfer personal property in only one way under the statute, a corporation is liable to the estate if it allows a transfer by an administrator who has not complied with the law.[4] It is sometimes provided by statute that such transfer shall be void. It was held in Massachusetts that a sale by an equitable owner of stock held by trustees under a trust agreement conveys the vendor's interest subject to the execution of the trust, and is not within the provisions of a

[1] Winter v. Montgomery, etc., Co., 89 Ala. 544, Wilgus' Cases; Lowry v. Bank, Taney 310.

[2] First Nat'l Bank v. Nat'l Broadway Bank, 156 N. Y. 459, 42 L. R. A. 139; Anderson v. Blood, 152 N. Y. 285; 1 Story Eq. Jur., § 400; 2 Perry on Trusts, § 831.

[3] Lowry v. Bank, Taney 310; Stewart v. Firemen's etc., Co., 53 Md. 564. See Marbury v. Ehlen, 72 Md. 206, 20 Am. St. Rep. 467.

[4] Citizens', etc., R. Co. v. Robbins, 128 Ind. 449.

statute which renders void every contract for the sale of stock "unless the party contracting to sell or transfer the same is at the time of making the contract the owner or assignee thereof, or authorized by the owner or assignee to sell or transfer it."[1]

§ 455. **Transfers in breach of trust—Liability of corporation.**—As a general rule a corporation may safely assume that the person in whose name shares stand on the books of the corporation is the owner thereof and entitled to sell and transfer the same, and receive the benefits resulting from such ownership. Unless the corporation has actual or constructive notice of the fact that the holder of the legal title is not the actual and beneficial owner it may safely register a transfer without danger of liability to beneficiaries or equitable owners.[2] But the corporation in many respects occupies the position of a trustee for its stockholders, and is responsible for any injuries sustained by the beneficial owner through its negligence. Thus, where the corporation had notice of the facts that the shares of stock in question were held by A as trustee for B under an indenture of trust which authorized the trustee to sell and reinvest the trust property only upon obtaining the written consent of the *cestui que trust*, the corporation was held liable to B for permitting a transfer of the shares without her consent without making due inquiry as to the authority of the trustee. An examination of the powers of the trustee would have revealed the fact that he had no authority to make the transfer and the failure to make the inquiry was negligence. The court said:[3]

[1] Duchemin v. Kendall, 149 Mass. 171, 3 L. R. A. 784.

[2] Smith v. Nashville, etc., R. Co., 91 Tenn. 221; Read v. Cumberland, etc., Co., 93 Tenn. 482. The corporation is required to exercise only ordinary care and diligence to protect its stockholders against unauthorized transfers. Caulkins v. Gas, etc., Co., 85 Tenn. 683, 4 Am. St. Rep. 786.

[3] Loring v. Salisbury Mills, 125 Mass. 138; Bird v. Chicago, etc., R. Co., 137 Mass. 428; Tafft v. Presidio, etc., R. Co., 84 Cal. 131; Shaw v. Spencer, 100 Mass. 382; Fisher v. Brown, 104 Mass. 259; Bohlen's Estate, 75 Pa. St. 304; Porter v. Bank of Rutland, 19 Vt. 410; Bayard v. Farmers' Bank, 52 Pa. St. 232; Parrott v. Byers, 40 Cal. 614; Caulkins v. Gas, etc., Co., 85 Tenn. 683; Railroad Co. v. Humphries (Miss.), 7 So. Rep. 522; Marbury v. Ehlen, 72 Md. 206. "An unauthorized transfer may work a serious wrong to

"When the holder of a certificate of shares in a corporation is the absolute owner, his assignment and delivery thereof will pass the title to the assignee; and the latter, upon surrendering the former certificate, may obtain a new one in his own name. If the holder appears on the face of the old certificate to be the absolute owner, and the corporation has no notice that the fact is otherwise, it may safely issue a new certificate to the assignee which, if taken in good faith and for a valuable consideration, will vest and perfect the title in him. But for the protection of the rights of the lawful owner of the shares the corporation is bound to use reasonable care in the issue of certificates; if by the form of the certificate or otherwise the corporation has notice that the present holder is not the absolute owner, but holds the shares by such a title that he may not have authority to transfer them, the corporation is not obliged, without evidence of such authority, to issue a certificate to his assignee, and if without making any inquiry it does issue a new certificate, and the rightful owner is injured by its negligence and wrongful act, the corporation is liable to him without proof of fraud or collusion. All the authorities affirm such liability where the corporation has notice that the present holder is a trustee and of the name of his *cestui que trust*, and issues a new certificate without making any inquiry whether his trust authorizes him to make a transfer." The fact that the certificate shows on its face that the holder is a trustee or executor is sufficient to put the corporation upon inquiry as to the extent of his powers.[1] The taking up of a stock certificate by the corporation from one to whom a life estate therein has been bequeathed, upon the presentment of the certificate with an indorsement by the executors that they have sold the stock to the life tenant, without inquiry as to whether there was an ac-

the equitable owner, and if the corporation allows it to be made with notice of the want of authority, or if put upon inquiry, without proper investigation into the authority, it becomes a party to the wrong." Peck v. Bank of America, 16 R. I. 710.

[1] Shaw v. Spencer, 100 Mass. 382. See Brewster v. Sime, 42 Cal. 139; Bank v. Cady, L. R. 15 A. C. 267.

tual sale for value, is such negligence as will render the corporation liable for injuries resulting to the remainderman.[1]

§ 456. **When the power to sell exists—Presumption of right doing.**—It is more difficult to determine the liability of the corporation when the trustee has authority to sell the shares, but in fact transfers them for the purpose of misappropriating the proceeds, or as a pledge to secure his own debt. A holds stock in trust for B, with power to sell the same at his discretion, and exchange for other securities. C is the custodian of the stock with knowledge of A's trust, and also of his power to sell. C permits A by his lawfully constituted attorney to transfer a part of the stock on the books of the corporation to another bank. The transfers were in fact by way of pledge to secure the individual debt of the attorney, and were made without authority and in fraud of the rights of B. C had no knowledge of the wrongful act of A's attorney, except in so far as it was imputed from the fact that he knew that A held the stock in the manner aforesaid. Under these circumstances the supreme court of Rhode Island held that C was not guilty of negligence in permitting the transfer to be made, as it had the right to presume that the transfer was made in pursuance of the authority contained in the will, and not in fraud thereof.[2] "The power of the trustee to sell the stock, coupled with the presumption that she was acting honestly, and in pursuance of that power, made the transfer apparently rightful, or at any rate the act, under the circumstances, was not such as ought to cause a reasonably prudent man to suspect that it was wrongful. Ordinary diligence, and not suspicious watchfulness, is the measure of duty which a corporation owes to its stockholders in such cases. In this case we do not see that either suggestion of danger or ground of suspicion exists."

[1] Cox v. First Nat'l Bank, 119 N. C. 302.

[2] Peck v. Providence, etc., Co., 17 R. I. 275. See, also, Peck v. Bank, etc., Co., 16 R. I. 710.

§ 457. **Lien of corporation upon shares.**—A corporation has no lien upon the shares of its members for debts due it unless it is created or authorized by the charter or statute, or by agreement of the parties.[2] Under authority to regulate transfers by the weight of authority a lien may be created by a by-law adopted by a majority of the shareholders,[3] which will be valid as against stockholders and purchasers with notice, but there is much authority to the contrary. Where a lien is created by the charter or by a general law, all persons purchasing shares are bound by it, and the corporation may refuse to transfer the shares until its claim is satisfied,[4] but if it is created by a by-law it does not bind a purchaser without notice.[5] When the law gives to a corporation a lien on the shares for any debt due the bank from the owner, it has a vested right in the shares which can not be divested by a subsequent assignment thereof by the shareholder.[6] The lien is not confined to debts growing out of the original subscrip-

[1] See Cook on Corps., 4th ed., § 522, and cases cited from Alabama, California, New York, Louisiana, Massachusetts, Missouri, Mississippi and Pennsylvania.

[2] Gemmell v. Davis, 75 Md. 546; Dearborn v. Washington Sav. Bank, 18 Wash. 8; Case v. Bank, 100 U. S. 446; Merchants Bank v. Shouse, 102 Pa. St. 488; Driscoll v. West Bradley, etc., Co., 59 N. Y. 96; Williams v. Lowe, 4 Neb. 382; Vansands v. Middlesex, etc., Bank, 26 Conn. 144; Sargent v. Insurance Co., 8 Pick. (Mass.) 90; Farmers', etc., Bank v. Wasson, 48 Iowa 336; Bank v. Lanier, 11 Wall. (U. S.) 369. When no restriction is placed by law on the transfer of corporate stock, a purchaser of such stock is not affected by any contractual restrictions on the power of transfer of which he had no notice. Brinkerhoff, etc., Co. v. Home, etc., Co., 118 Mo. 447, Wilgus' Cases.

[3] Lockwood v. Mechanics Nat'l Bank, 9 R. I. 308; Morgan v. Bank, 8 Serg. & R. (Pa.) 73; Vansands v. Bank, 26 Conn. 144; Planters', etc., Bank v. Selma, etc., Bank, 63 Ala. 585.

[4] Union Bank v. Laird, 2 Wheat. (U. S.) 390; Bishop v. Globe Co., 135 Mass. 132; Oakland, etc., Bank v. State Bank, 113 Mich. 284; John C. Graffin Co. v. Woodside, 87 Md. 146.

[5] Driscoll v. West Bradley, etc., Co., 59 N. Y. 96; Anglo-California Bank v. Grangers' Bank, 63 Cal. 359; Bishop v. Globe Co., 135 Mass. 132; Bank of Atchison v. Durfee, 118 Mo. 431; Brinkerhoff, etc., Co. v. Home, etc., Co., 118 Mo. 447, Wilgus' Cases; Oakland, etc., Bank v. State Bank, 113 Mich. 384.

[6] Geo. H. Hammond Co. v. Hastings, 134 U. S. 401; Prince, etc., Co. v. St. Paul, etc., Co., 68 Minn. 121; Bank of Commerce v. Bank of Newport, 11 C. C. A. 484, 63 Fed. Rep. 898; Jennings v. Bank, 79 Cal. 323, 5 L. R. A. 233; Mohawk Nat'l Bank v. Schenectady Bank, 28 N.Y. Supp. 1100, 78 Hun 96.

tion and subsequent calls and assessments. It includes a debt which results from the wrongful use of the money of the corporation by its secretary, who was also a stockholder.[1] A stockholder, who, with notice of a by-law which provides that no stockholder owing the corporation a matured debt, shall transfer his stock, or receive a dividend thereon until the debt is paid, contracts a debt to the corporation, will be held to have pledged his stock to the corporation, and the pledge is binding as between the corporation and the assignee of the stockholder.[2] The character and extent of the lien is determined by the terms of the provision creating it. When the statute gives the corporation a lien upon the stock at all times "for all the debts due from them [the stockholders] to such corporation," the lien attaches for debts incurred before the acquisition of the stock.[3] The word "debt" includes the liability on a note not due,[4] and "indebted" includes the collateral liability of a surety.[5] But such provisions do not prevent an assignment of the equitable interest in the shares, subject to the rights of the corporation.[6] The corporation may waive its lien by allowing a transfer on its books,[7] or by inducing a purchaser to act upon the statement that there are no claims against the stock.[8] The mere taking of other security is not a waiver of the lien.[9] But the failure to put a copy of the by-laws in a conspicuous place, as required by the statute, will defeat a lien conferred by the by-law, as against a good-faith transfer of the shares without knowledge of the by-law.[10] A national bank can not acquire a lien on its own shares for debts from its stockholders to the bank.[11]

[1] National Bank v. Rochester, etc., Co., 172 Pa. St. 614.

[2] John C. Graffin Co. v. Woodside, 87 Md. 146.

[3] Schmidt v. Hennepin, etc., Co., 35 Minn. 511.

[4] Grant v. Mechanics Bank, 15 Serg. & R. 140; Pittsburgh, etc., R. Co. v. Clarke-Thaw, 29 Pa. St. 146.

[5] St. Louis, etc., Co. v. Goodfellow, 9 Mo. 149; Leggett v. Bank, 24 N.Y. 283.

[6] National Bank v. Watsontown Bank, 105 U. S. 217; Moore v. Bank of Commerce, 52 Mo. 377.

[7] Hill v. Pine River Bank, 45 N. H 300.

[8] National Bank v. Watsontown Bank, 105 U. S. 217; Bishop v. Globe Co., 135 Mass. 132.

[9] German Nat'l Bank v. Kentucky T. Co. (Ky.), 40 S. W. Rep. 458.

[10] Des Moines Nat'l Bank v. Bank, 97 Iowa 204.

[11] Bullard v. Bank, 18 Wall. (U.S.) 589.

It has been held that the identity of the shares is not affected by their transfer and that a stockholder is entitled to have the shares transferred although, at the time, subject to a lien for a delinquent assessment; the lien is not affected, but continues.[1] A corporation which has knowledge of a pledge of stock can not extend credit to the stockholder and thus acquire a lien on the stock under a statute which provides that transfers or liens affecting the stock if not made or registered upon the books of the corporation are invalid as to subsequent purchasers without notice.[2] The lien is for debts incurred in good faith and can not be asserted against a prior claim to the stock by a third person of which the corporation had notice at the time the debt was contracted although the stock had not then been transferred on the books of the corporation.[3] But the lien given by statute is of course not affected by the mere sale of the stock to an innocent purchaser.[4] So a corporation with knowledge that stock has been pledged acquires no lien on the stock which is prior to the lien of the pledgee for a debt resulting from an embezzlement by its stockholder who is its president.[5] The lien of the corporation can not be foreclosed by a bill in equity when there is an adequate remedy by execution and sale of the shares.[6]

§ 458. **Effect of a transfer upon rights and liabilities of parties.**—The legal effect of a complete transfer of shares is a novation of parties. When the transfer is properly and legally made, the transferrer is discharged from any further liability by reason of his ownership of the shares, unless the liability is continued under statutory provisions.[7] If the shares are not fully paid up, the transferee becomes liable for all calls made during his ownership, and the transferrer remains liable for

[1] Craig v. Hesperia, etc., Co., 113 Cal. 7.

[2] Birmingham, etc., Co. v. Bank (Ala.), 20 L. R. A. 600.

[3] Prince, etc., Co. v. St. Paul, etc., Co., 68 Minn. 121.

[4] George H. Hammond & Co. v. Hastings, 134 U. S. 401; Bank of Commerce v. Bank, 27 U. S. App. 486, 63 Fed. Rep. 898.

[5] Hotchkiss, etc., Co. v. Union Nat'l Bank, 37 U. S. App. 86.

[6] Aldine, etc., Co. v. Phillips (Mich.), 42 L. R. A. 534, 76 N. W. Rep. 371.

[7] Rochester, etc., Co. v. Raymond, 158 N. Y. 576, 53 N. E. Rep. 507.

calls which were duly made before the transfer.[1] The transferee can not defend an action for assessments by showing that the original subscription was induced by fraud.[2] Ordinarily the transferee becomes liable for any amount unpaid on the subscription;[3] but, as against the corporation, he is not liable when the certificate asserts that the stock is full paid,[4] and he is an innocent purchaser of the shares for value;[5] the transferrer in this event probably continues liable, at least to creditors.[6] As the transferee assumes the subsequent calls, he becomes entitled to all dividends subsequently declared.[7]

"Stockholders are," says Judge Jenkins,[8] "as to property of the corporations, quasi partners, holding *per my et per tout.* The earnings of the corporation are part of the corporate property, held by the same tenure, and until separated from the general mass, the interest of the stockholders therein passes with a transfer of the stock, and this, irrespective of the time during which earnings have accrued. By the declaration of a dividend, however, the earnings, to the extent declared, are separated from the general mass of property and appropriated to the then stockholders, who become creditors of the corporation for the amount of the dividend. The relationship of the stockholder to the corporation, as to the amount of the dividend, is thus changed from one of partnership ownership, to

[1] Webster v. Upton, 91 U. S. 65; Hartford, etc., R. Co. v. Boorman, 12 Conn. 530. As to the release of the transferrer from further liability, see White v. Green, 105 Iowa 176; Herrick v. Wardwell, 58 Ohio St. 294; Russell v. Easterbrook, 71 Conn. 50. As to liability of transferee, White v. Marquardt & Sons, 105 Iowa 145; Harper v. Carroll, 66 Minn. 487; Sturtevant v. National, etc., Works, 88 Fed. Rep. 613, 60 U. S. App 235.

[2] Lewis v. Berryville, etc., Co., 90 Va. 693; Cardwell v. Kelly, 95 Va. 570, 40 L. R. A. 240.

[3] Bell's App., 115 Pa. St. 88, 2 Am. St. Rep. 532.

[4] Appeal of Kisterbock, 127 Pa. St. 601, 14 Am. St. Rep. 868. § 322.

[5] West Nashville, etc., R. Co. v. Nashville, etc., Bank, 6 Am. St. Rep. 835. As to effect of a printed statement on the certificate as notice, see Jennings v. Bank, 79 Cal. 323, 12 Am. St. Rep. 145; Brant v. Ehlen, 59 Md. 1.

[6] Taylor Corps., § 702, citing Boynton v. Hatch, 47 N. Y. 225; Tallmadge v. Fishkill, etc., Co., 4 Barb. (N. Y.) 382; Pell's Case, L. R. 5 Ch. 11. But see Christensen v. Eno, 106 N. Y. 97.

[7] Supply, etc., Co. v. Elliott, 10 Colo., 327, 3 Am. St. Rep. 586, and note; Libby v. Tobey, 82 Maine 397; Lippitt v. American, etc., Co., 15 R. I. 141.

[8] Wheeler v. Northwestern, etc., Co., 39 Fed. Rep. 347. See § 398, *et seq.*

that of creditor. He thereafter stands to the corporation in a dual relation,—with respect to his stock, as partner and part owner of the corporate property, with respect to the dividend as creditor upon a par with other creditors of the corporation. The severance of the earnings from the general mass of corporate property, and the promise to pay, arising from the declaration of the dividend, works this change. The earnings represented by the dividend, although the fruit of the general property of the company, are no longer represented by the stock, but become a debt of the company to the individual who, at the time of the declaration of dividend, was the owner of the stock. That the dividend is payable at a future date can work no distinction in the right. The debt exists from the time of the declaration of dividend, although payment is postponed for the convenience of the company. The right became fixed and absolute by the declaration. This right could, of course, be transferred with the stock by special agreement, but not otherwise. The dividend would not pass as an incident of the stock.[1] * * * The dividends are earnings growing out of the stock, but when declared are immediately separated from it, and exist independently of it. They are happily likened * * * to fallen fruit which does not pass with the sale or gift of the tree."

§ 459. **Remedies for a wrongful refusal to transfer.**[2]—When the corporation wrongfully refuses to permit the registry on its books of a transfer of shares, the party entitled to the transfer may either bring an action for damages or a bill in equity to compel the transfer, and in some jurisdictions he will be entitled to a mandamus.

§ 460. **An action for damages.**—The usual remedy is an action for damages and when new shares can be purchased in the market it is reasonably adequate. There is some conflict among the authorities as to the proper measure of damages in case of a conversion of shares by a refusal to permit a transfer

[1] Brundage v. Brundage, 60 N. Y. 544; Hill v. Newichawanick Co., 8 Hun 459, affirmed 71 N. Y. 593; Boardman v. Railway Co., 84 N. Y. 157.

[2] See Wilgus' Cases.

to be registered. One group of cases holds that the measure of damages is the market value of the shares at the time of the conversion,[1] in accordance with the general rule for the measure of damages for the conversion of personal property. "In the absence of special circumstances in an action for conversion of personal property as well as one for failure to deliver it in performance of a contract where consideration has been received, the value of the property at the time of such conversion or default, with interest, is the measure of compensation."[2] A few cases hold that the measure of damages is the value of the shares on the day of the trial,[3] while a third class holds that it is the highest market price reached by the shares between the time of the refusal to permit the transfer and the day of the trial.[4]

§ 461. **A suit in equity.**—Another remedy of which the party may avail himself is a suit in equity to compel a trans-

[1] Hussey v. Manufacturers, etc., Bank, 10 Pick. 415; Barnes v. Brown, 130 N. Y. 372; North v. Phillips, 89 Pa. St. 250; Work v. Bennett, 70 Pa. St. 484; Baker v. Drake, 66 N. Y. 518; Colt v. Owens, 90 N. Y. 368; Pinkerton v. Manchester, etc., R. Co., 42 N. H. 424; McKenney v. Haines, 63 Maine 74; Doty v. First Nat'l Bank, 3 N. D. 9, 53 N. W. Rep. 77; Rio Grande, etc., Co. v. Burns, 82 Texas 50, 17 S. W. Rep. 1043; Gresham v. Island City, etc., Bank (Texas Civ. App., 1893), 21 S. W. Rep. 556; Kortright v. Buffalo, etc., Bank, 20 Wend. 90; Nicollet, etc., Bank v. City Bank, 38 Minn. 85. See Balkis, etc., Co. v. Tompkinson, L. R. (1893) A. C. 396.

[2] Barnes v. Brown, 130 N. Y. 372.

[3] Owen v. Routh, 14 C. B. 327; Bercich v. Marye, 9 Nev. 312.

[4] Fromm v. Sierra Nevada, etc., Co., 61 Cal. 629; Dent v. Holbrook, 54 Cal. 145; Douglass v. Kraft, 9 Cal. 562. See Kid v. Mitchell, 1 Nott. & McC. 334; Central, etc., Co. v. Atlantic, etc., R. Co., 50 Ga. 444. This was the rule established by the early New York cases. Markham v. Jaudon, 41 N. Y. 235; Kortright v. Buffalo, etc., Bank, 20 Wend. 90; Romaine v. VanAllen, 26 N. Y. 309, but in the more recent cases the general rule is adopted that the measure of damages is the value at the date of the conversion. Baker v. Drake, 66 N. Y. 518; Harris v. Tumbridge, 83 N. Y. 92.

[5] Morehead v. Western, etc., R. Co., 96 N. C. 362, 2 S. E. Rep. 247; Livezey v. N. P. R. Co., 157 Pa. St. 75; Archer v. Water-works Co., 50 N. J. Eq. 33; Slemmons v. Thompson, 23 Ore. 215, 31 Pac. Rep. 514; Cushman v. Thayer, etc., Co., 76 N. Y. 365; Walker v. Detroit, etc., R. Co., 47 Mich. 338; Iasigi v. Chicago, etc., R. Co., 129 Mass. 46; Campbell v. American, etc., Co., 122 N. Y. 455; Hill v. Atoka, etc., Co. (Mo., 1893), 21 S. W. Rep. 508; Gould v. Head, 41 Fed. Rep. 240; Rice v. Rockefeller, 131 N. Y. 174,

fer.[5] "To say that the holder shall not be entitled to the stock because the corporation, without any just reason, refuses to transfer it, and that he shall be left to pursue the remedy of an action for damages, in which he can recover only a nominal amount, would establish a rule which must work great injustice in many cases, and confer a power on corporate bodies which has no sanction in the law. A court of equity will enforce a specific performance on a contract for the sale of real estate, and compel the execution of a deed by the vendor to the vendee, although an action at law may be brought to recover damages for the breach of the contract. Such a case bears a striking analogy to the one now presented, and the same principle is manifestly applicable when the remedy in law is inadequate to furnish the proper relief."[1] The bill may be in the alternative for a transfer of the stock or for damages.[2]

§ 462. **Mandamus.**—The great weight of authority is against the rule that mandamus will lie to compel the registry of a transfer of shares. The reason for denying this remedy is thus stated: "The applicants have an adequate remedy, by a spe-

Wilgus' Cases. Suit for specific performance. New England, etc., Co. v. Abbott, 162 Mass. 148.

[1] Cushman v. Thayer, etc., Co., 76 N. Y. 365. "This is, it seems, the surest, most complete and most just remedy for compelling a corporation to register a transfer of stock, and for adjusting the various conflicting rights or claims of other parties." Cook I, § 391. "A contract for the sale of shares will be specially enforced in equity if it is not unconscionable (Miss. & M. R. Co. v. Cromwell, 91 U. S, 643), or against public policy, when from the scarcity of the shares or other reasons the purchaser can not go into the market and purchase similar ones. Johnson v. Brooks, 93 N. Y. 337. But if shares similar to the ones which are the subject of the sale are readily purchasable in the market, equity will not, as a general rule, specifically enforce the contract, but will leave the parties to their remedy at law. Ross v. U. P. R. Co., 1 Woolw. C. C. 26." Taylor, § 790. See Folls' Appeal, 91 Pa. St. 434. "In such a case it is well settled that, although the common law remedy for damages is available, it is inadequate; the only effective remedy is an order of the court of equity to compel such officers to make transfer of the stock on the books of the company to the assignee, and thus enable such assignee to enjoy all the rights of the stockholder in such corporation, and likewise to compel such officers to issue new certificates of stock upon the surrender of the old ones." Tiedeman Eq. Jur., § 504.

[2] Birmingham Nat'l Bank v. Roden, 97 Ala. 404, 11 So. Rep. 883; In re Reading Iron Works, 149 Pa. St. 182, 24 Atl. Rep. 202.

cial action on the case, to recover the value of stock if the bank has unduly refused to transfer it. There is no need of the extraordinary remedy by mandamus in so ordinary a case. It might as well be required in every case where trover would lie. It is not a matter of public concern, as in the case of public records and documents, and there can not be any necessity or even a desire of possessing the identical shares in question."[1] As said by one writer:[2] "Shares of stock in a trading corporation are supposed to possess a market value which may be made the basis for calculating the measure of damages for the losses resulting from a failure or refusal to enter their transfer on the registry of the corporation. Mandamus is therefore seldom granted to compel their transfer." But there are many authorities[3] which hold that mandamus will lie, par-

[1] Shipley v. Mechanic's Bank, 10 John. 484; State v. Rombauer, 46 Mo. 155; Stackpole v. Seymour, 127 Mass. 104; Townes v. Nichols, 73 Me. 515; Gray v. Portland Bank, 3 Mass. 364; Murray v. Stevens, 110 Mass. 95; Baker v. Marshall, 15 Minn. 177 (Gill. 136); Tobey v. Hakes, 54 Conn. 274; Burnsville, etc., Co. v. State, 119 Ind. 382; Freon v. Carriage Co., 42 Ohio St. 30; Kimball v. Union, etc., Co., 44 Cal. 173; Bank of Ga. v. Harrison, 66 Ga. 696.

[2] Spelling Extraordinary Relief, II, § 1615.

[3] State v. McIver, 2 S. C. (N. S.) 25; State v. Cheraw, etc., R. Co., 16 S. C. 524; In re Klaus, 67 Wis. 401; Green Mount, etc., Co. v. Bulla, 45 Ind. 1; People v. Goss, etc., Co., 99 Ill. 355; State v. First Nat'l Bank, 89 Ind. 302; People v. Crockett, 9 Cal. 112; Crawford v. Prov., etc., Co., 8 U. C. (C. P.) 263; Goodwin v. Ottawa, etc., R. Co., 13 U. C. (C. P.) 254; Slemmons v. Thompson, 23 Ore. 215, 31 Pac. Rep. 514; Campbell v. Morgan, 4 Ill. App. 100; Norris v. Irish, etc., Co., 8 El. & Bl. 512; Ward v. S. E. R. Co., 2 El. & El. 812; Ex parte Sargent, L. R. 17 Eq. 273. "There is not wanting strong authority, both in numbers and eminence, for the doctrine that rightful registry may be compelled by mandamus. When this is the rule, a demand by letter is sufficient, and the writ may issue upon noncompliance therewith. State v. McIver, 2 S. C. 25. But mandamus will not be granted where the relator is guilty of bad faith, Reg. v. Liverpool, etc., Co., 21 L. J. Q. B. (N. S.) 284, nor where the certificates have been issued to another whose rights would be prejudiced. Bailey v. Strohecker, 38 Ga. 259; State v. First Nat'l Bank, 89 Ind. 302; Durham v. Mon., etc., Co., 9 Ore. 41, unless, indeed, the applicant shows a better title. Reg. v. Charwood, etc., Co., 1 C. & F. 419, nor even where the duty to register is prescribed by statute, unless the applicant's right to possession is clear and unquestionable. Slemmons v. Thompson, 23 Ore. 215, 31 Pac. Rep. 514. Compare, Bangor, etc., Co. v. Robinson, 52 Fed. Rep. 520." Spelling says that there is

ticularly where there appears to be no good reason why the registry of the transfer should not be allowed.

an exception to the general rule that mandamus will not lie, when by statute it is made the plain ministerial duty of the corporation to make the proper entries of a transfer after the sale of shares on execution against the original shareholder. Extr. Relief, II, § 1616.

CHAPTER 17.

CORPORATE MEETINGS AND ELECTIONS.

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§ 463. **In general.**—The powers which are conferred upon a corporation can be exercised only at a regularly convened meeting of the stockholders or of the board of directors; and the action of individual stockholders or directors elsewhere than at a properly convened meeting does not bind the corporation, unless it is subsequently ratified by proper authority.[1]

[1] Buttrick v. Nashua, etc., R., 62 N. H. 413, 13 Am. St. Rep. 578; Gashwiler v. Willis, 33 Cal. 11; Alta, etc., Co. v. Alta, etc., Co., 78 Cal. 629; People's Bank v. St. Anthony's, etc., R.C.Church, 39 Hun (N.Y.) 498; North Hudson, etc., Assn. v. Childs, 82 Wis. 460; Sayles v. Brown, 40 Fed. Rep. 8. In Longmont, etc., Co. v. Coffman, 11 Colo. 551, it is held that where a

For certain purposes it is held that the action of all the stockholders will bind the corporation, although they acted individually and not at a regular meeting.[1] But this is exceptional, and the general rule is as stated above. Thus, the consent of a majority of the stockholders to the appointment of an agent of the corporation to execute a mortgage, given separately and at different times, is ineffective; and a mortgage executed by one assuming to act as an agent under such an appointment is a nullity.[2] A strictly corporate meeting, that is, a meeting of the stockholders, must be distinguished from a meeting of the board of directors, which ordinarily exercises the general powers conferred upon the corporation.

§ 464. **Calling meetings.**—Unless otherwise provided by the charter or by-laws, a corporate meeting may be called by the directors, or the general agent of the corporation to whom is entrusted the control and management of its affairs, whenever in their judgment a meeting is necessary.[3] If the manner of calling such meetings is determined by the charter or by-laws, a meeting called in any other way is invalid unless all the stockholders are present.[4] The board of directors, however, it has been held, may call a meeting, although the by-laws confer the power upon other officers.[5] Where the authority is vested in the trustees or directors, the president can not call a meeting to elect officers.[6]

§ 465. **The place of meeting.**—A corporate meeting must be held at a time or place which is reasonably convenient for the shareholders who are expected to attend it. It is ordi-

majority of the board of directors acting separately in accordance with usage, approved claims against the corporation, the corporation is bound by the act.

[1] See Woodbridge v. Pratt, etc., Co., 39 Conn. 304, 37 Atl. Rep. 688.

[2] Duke v. Markham, 105 N. C. 131.

[3] Stebbins v. Merritt, 10 Cush. 27, 33.

[4] See Evans v. Osgood, 18 Me. 213.

[5] Citizens', etc., Co. v. Sortwell, 8 Allen (Mass.) 217. See Chamberlain v. Painesville, etc., R. Co., 15 Ohio St. 225.

[6] State v. Pettineli, 10 Nev. 141. Statutes sometimes provide for a proceeding by which a meeting may be called by a justice of the peace when the proper officers are absent. See Gen. St. Minn. 1894, § 3409.

narily held at the office of the corporation.[1] There is some question as to the validity of acts done at a stockholders' meeting held outside of the state which created the corporation. On the ground that such a meeting is a strictly corporate, as distinguished from a business act, it has been broadly held that the transactions of such a meeting are void, although there is no express prohibition in the charter or by-laws, and all the members consent. "As the corporate faculty can not accompany the natural person beyond the bounds of the sovereignty which confers it, and they can not possess or exercise it there, they can have no more power there to make the artificial being act than other persons not named as associates or incorporators. Any attempt to exercise such a faculty there is merely a usurpation of authority by persons destitute of it, and acting without any legal capacity to act in that manner. It follows that all votes and proceedings of persons professing to act in the capacity of corporators, when assembled without the bounds of the sovereignty granting the charter, are wholly void."[2] If such a meeting is expressly prohibited it is illegal, but in the absence of such a prohibition there appears to be no very good reason why the shareholders of an ordinary business corporation should not provide in their articles that meetings may be called at convenient places outside of the state under whose laws the company is formed.[3]

If the meeting is not prohibited, and all the stockholders consent, it will generally be treated as merely irregular and the transaction binding upon all parties.

Where an Illinois corporation held a meeting and elected directors in Missouri, and certain stockholders attempted to defeat an action on their stock subscriptions on the ground that the proceedings of the meeting in Missouri at which the

[1] The office of the president will be presumed to be the proper place for holding a meeting. Troy, etc., Co. v. White, 10 S. Dak. 475, 42 L. R. A. 549.

[2] Miller v. Ewer, 27 Me. 509. See § 247, *supra*. Ormsby v. Vermont, etc., Co., 56 N. Y. 623; Franco-Texan, etc., Co. v. Laigle, 59 Tex. 339; Duke v. Taylor, 37 Fla. 64, 31 L. R. A. 484. Conferring authority upon an agent to execute a deed is not a corporate act. Arms v. Conant, 36 Vt. 744; Bellows v. Todd, 39 Ia. 209.

[3] See Morawetz Priv. Corp., § 488.

call was made were void, the court said:[1] "The utmost that can be said, under such circumstances, is that the election was irregular. The corporation having once been put into existence, if the members of the board of directors, whether charter or their appointees, or those elected by the stockholders in St. Louis, accepted their office, and acted under their appointment or election, as the evidence shows was the case, they become *de facto* directors, and their authority to act on behalf of the corporation could not be questioned by the appellants in this collateral suit without showing a judgment of ouster against them in a direct proceeding by the government for that purpose."

In some states stockholders' meetings held in another jurisdiction are forbidden by law. Where the by-laws provided that the meetings should be held at a designated place in the state it was held that a meeting for the election of officers held out of the state, all the stockholders not consenting, was illegal and the election void.[2]

The corporation itself and the stockholders who attend an extraterritorial meeting, and creditors who voluntarily deal with the corporation, are estopped to deny its validity and regularity.[3] As against officers elected at an illegal meeting

[1] Ohio, etc., R. Co. v. McPherson, 35 Mo. 13.

[2] Hodgson v. Duluth, etc., R. Co., 46 Minn. 454.

[3] Wright v. Lee, 2 S. Dak. 596, 51 N. W. Rep. 706.

In Handley v. Stutz, 139 U. S. 417, the court said: "Nor were the proceedings of such meeting any the less binding upon those participating in it by reason of the fact that it was held without call or notice, and outside the boundaries of the state under the laws of which the company was incorporated. * * * Beyond the election of officers, however, there is no statutory restriction of corporate action to the limits of the state, and in the absence of such inhibition the proceedings of such meeting would, within the rule laid down by this court in Galveston, etc., R. Co. v. Cowdrey, 11 Wall. 459, with regard to directors' meetings, be binding upon all those participating in, as well as upon those acting upon the faith of its validity, on receiving stock authorized to be issued at such meeting. It is true that there are cases holding that stockholders' meetings can not be legally held outside of the home state of the corporation, but the question has generally arisen where a majority present at such meeting has attempted by their action to bind a dissenting minority, or had taken action prejudicial to the rights of third persons. Ormsby v. Vermont, etc., Co., 56

held outside of the state, those previously in office retain the right to control the affairs of the corporation.[1]

When a corporation is incorporated in several states a meeting in one of the states in respect of the property in that state is valid without a repetition of the meeting in the other states.[2]

§ 466. **Regular and special meetings.**—The charter or by-laws of a corporation ordinarily provide a time for holding regular meetings and for the calling of special meetings. The difference is of importance by reason of the necessity for special notice of special meetings.

§ 467. **Notice of corporate meeting.**—No power or function entrusted to a body consisting of a number of persons can be legally exercised without notice to all the persons composing such body.[3] Hence there can be no valid stockholders' meeting unless all the shareholders have had proper notice of the day, hour and place of meeting.[4] Notice will be presumed until the contrary appears.[5] If the time for the regular meeting is fixed by charter, by-law,[6] or by usage,[7] no other notice is necessary.[8] If a by-law fixes merely the day of a meeting,

N. Y. 623; Hilles v. Parrish, 14 N. J. Eq. 380. Indeed, so far as we know, the authorities are uniform to the effect that the action taken at such meeting is binding upon those who participated in or take the benefit of them. Heath v. Silverthorn, etc., Co., 39 Wis. 146."

[1] Hodgson v. Duluth, etc., Co., 46 Minn. 454.

[2] Graham v. Railroad Co., 118 U. S. 161.

[3] § 296, *supra*; People v. Batchelor, 22 N. Y. 128.

[4] San Buenaventura, etc., Co. v. Vassault, 50 Cal. 534; State v. Bonnell, 35 Ohio St. 10. In Am. Nat'l Bank v. Oriental Mills, 17 R. I. 551, 23 Atl. Rep. 795, it was held that it was sufficient to give the notice to the holder of the equitable title, the former holder having the bare legal title not coupled with an interest. Notice to the pledgor of shares is sufficient. McDaniels v. Flower Brook, etc., Co., 22 Vt. 274. Notice to one member of a firm is sufficient. Kenton, etc., Co. v. McAlpin, 5 Fed. Rep. 737.

[5] Sargent v. Webster, 13 Mete. 497; McDaniels v. Flower Brook, etc., Co., 22 Vt. 274.

[6] Morrill v. Little Falls, etc., Co., 53 Minn. 371, 21 L. R. A. 174; Warner v. Mower, 11 Vt. 385; State v. Bonnell, 35 Ohio St. 10.

[7] Atlantic, etc., Co. v. Sanders, 36 N. H. 252. See Wiggin v. Freewill Baptist Church, 8 Mete. (Mass.) 301.

[8] Morrill v. Manufacturing Co., 53 Minn. 371; State v. Bonnell, 35 Ohio St. 10; Stow v. Wyse, 7 Conn. 214, 18 Am. Dec. 99, and note; Warner v. Mower, 11 Vt. 385.

notice must be given of the hour. The notice must fix the exact hour[1] and place of meeting.[2] If the meeting is a special one, or the business of an extraordinary character,[3] such as a sale of the property of the corporation,[4] or the dissolution of the corporation,[5] the notice must also indicate the nature of the business to be transacted.[6] Notice of a general meeting need not state the business to be transacted.[7] A notice stating that the annual meeting will be held at a certain time and place, to act on the report of the directors and transact such other business as may be brought before the meeting, will not authorize an increase of the capital stock at the meeting under a statute which permits such increase "at any meeting called for the purpose."[8] At a special meeting only the particular business for which it was called can be transacted.[9] The notice must be served a reasonable time before the meeting.[10] The acts of a meeting at which all the stockholders are present is valid, although no notice of the meeting was given.[11] So the acts of a majority at a meeting which was not regularly called may be ratified at a subsequent meeting.[12]

§ 468. **Adjourned meetings.**—A meeting may adjourn from time to time without further notice to the shareholders,[13] and

[1] San Buenaventura, etc., Co. v. Vassault, 50 Cal. 534.

[2] Miller v. English, 21 N. J. L. 317.

[3] Warner v. Mower, 11 Vt. 385; People's, etc., Co. v. Westcott, 14 Gray 440.

[4] Stockholders, etc., v. Louisville, etc., R. Co., 12 Bush (Ky.) 62.

[5] St. Mary's, etc., Assn. v. Lynch (N. H.), 9 Atl. Rep. 98.

[6] Atlantic, etc., Co. v. Mason, 5 R. I. 463; Evans v. Heating Co., 157 Mass. 37, 31 N. E. Rep. 698; In re Bridgeport, etc., Co., L. R. 2 Ch. 191. A notice which states the object to be "to consider the question of an issue of bonds of the company, secured by a mortgage on its property," is sufficient to authorize the taking of a vote authorizing the giving of a mortgage, under a statute which required that the meeting should be called for that purpose.

[7] Warner v. Mower, 11 Vt. 385.

[8] Jones v. Concord, etc., R. Co., 67 N. H. 119. As to definiteness required in describing the business to be transacted, see Market, etc., R. Co. v. Hellman, 109 Cal. 571.

[9] Warner v. Mower, 11 Vt. 385.

[10] Cassell v. Lexington, etc., Co. (Ky.), 9 S. W. Rep. 502.

[11] Stutz v. Handley, 41 Fed. Rep. 531, s. c. 139 U. S. 417; Stebbins v. Merritt, 10 Cush. (Mass.) 27.

[12] Richardson v. Railroad Co., 44 Vt. 613.

[13] Smith v. Law, 21 N. Y. 296. In re Newcomb (N. Y.), 18 N. Y. Supp. 16.

the adjourned meeting is but a continuation of the meeting adjourned.[1] Corporations "may transact any business at an adjourned meeting which they could have done at the original meeting. It is but a continuation of the same meeting. Whether the meeting is adjourned without interruption for many days, or by adjournment from day to day, or from time to time, many days intervening, it is evident it must be considered the same meeting without any loss or accumulation of powers.[2] In order that notice of a prior meeting may extend and apply to a subsequent meeting, the latter must be held merely for the purpose of completing the unfinished business of the former.[3] The hour of adjournment should be definitely fixed and should be entered upon the minutes in order to affect the members absent from the first with notice of the adjourned meeting.[4] The president of a mining company has no authority to adjourn a meeting of the stockholders against their express will, because in his opinion a majority of the subscribed stock is not represented.[5]

§469. **Manner of conducting meetings.**—Members may conduct a corporate meeting in any manner convenient and agreeable to themselves, so long as they do not violate any of the provisions of their charter or by-laws. No particular formalities are required,[6] but the statutory or charter provisions must be observed.[7] By-laws regulating the manner of conducting a meeting and voting must be consistent with the charter and laws.[8]

§ 470. **Records—Evidence.**—The failure to enter a resolution passed at the stockholders' meeting in the minute book of

See Weston, etc., Co. v. Des Moines, etc., Bank 103 Iowa 455.

[1] State v. Cronan, 23 Nev. 437, 49 Pac. Rep. 41.

[2] Warner v. Mower, 11 Vt. 385; Smith v. Law, 21 N. Y. 296; People v. Batchelor, 22 N. Y. 128; Farrar v. Perley, 7 Maine 401.

[3] People v. Batchelor, 22 N. Y. 128.

[4] Thompson v. Williams, 76 Cal. 153.

[5] State v. Cronan, 23 Nev. 437.

[6] Sayles v. Brown, 40 Fed. Rep. 8; Philips v. Wickham, 1 Paige Ch. (N. Y.) 590; Downing v. Potts, 23 N. J. L. 66. In re Horbury, etc., Co., L. R. 11 Ch. Div. 109; Hughes v. Parker, 20 N. H. 58.

[7] People v. Peck, 11 Wend. (N. Y.) 604. The presiding officer or moderator need not be a stockholder unless it is required by statute. Stebbins v. Merritt, 10 Cush. (Mass.) 27.

[8] Commonwealth v. Woelper, 3 S. & R. (Pa.) 30; People v. Crossley, 69

the corporation does not affect its validity, as the corporate acts can generally be proved as well by parol as by the written entry.[1]

§ 471. **Who entitled to vote.**—The right to vote at corporate meetings, upon complying with reasonable rules and regulations, is an incident to the ownership of shares in private corporations. Hence, every shareholder has a right to at least one vote, and of this right he can not be deprived by legislation, unless the power was reserved before the stock was issued. If there are no provisions in the charter or by-laws regulating the matter, the right and manner of voting must be determined by the corporate meeting, and not by the presiding officer.[2] The corporation may, by properly adopted by-law, prohibit the transfer of the shares on the corporate books for a reasonable period prior to an election.[3] The general rule is that the stock books are prima facie evidence of who is entitled to vote, and as this is one of the objects for which the corporation is required to keep such books, it can not be required to go outside of the books in order to determine who it should recognize.[4] But the books are not, under all circumstances, conclusive evidence,[5] although the inspectors of election need not go behind them.[6] The general rule, however, has received so many modifications, that many states have found it necessary to regulate the matter by statutory provision.[7] The right to vote can not be impaired by a by-law enacted after the stockholder acquired his shares, unless un-

Ill. 195; Brewster v. Hartley, 37 Cal. 15; Camden, etc., R. Co. v. Elkins, 37 N. J. Eq. 273.

[1] Handley v. Stutz, 139 U. S. 417; Moss v. Averell, 10 N. Y. 449. See note on corporate records in Sawyer v. Manchester, etc., R. Co. (N. H.), 13 Am. St. Rep. 550–552; Schell v. Second Nat'l Bank, 14 Minn. 43 (Gil. 34).

[2] State v. Chute, 34 Minn. 135.

[3] In re Glenn Salt Co., 17 App. Div. 234, 153 N. Y. 688.

[4] Hoppin v. Buffum, 9 R. I. 513; State v. Ferris, 42 Conn. 560; In re Long Island, etc., R. Co., 19 Wend. 38; Prince Inv. Co. v. St. Paul, etc., Co., 68 Minn. 121; In re Argus Pt. Co. (N. Dak.), 48 N. W. Rep. 347. That the corporate books are conclusive, see Morrill v. Little Falls, etc., Co, 53 Minn. 371, 21 L. R. A. 174.

[5] Strong v. Smith, 15 Hun (N.Y.) 222.

[6] In re St. Lawrence, etc., Co., 44 N. J. L. 529.

[7] Ex parte Willcocks, 7 Cowen (N.Y.) 402; Commonwealth v. Dalzell, 152 Pa. St. 217, 34 Am. St. Rep. 640; McNeil v. Tenth Nat'l Bank, 46 N. Y.

der reserved power.[1] The corporation may at the time of issuing the shares, provide that the holder shall not participate in the management of the corporation.[2] Thus, it is not uncommon for the charter or statute to provide that non-resident stockholders shall not be entitled to vote.[3] Under such circumstances, the provision can not be evaded by a gratuitous transfer of the shares to some other party.[4] The holder of the legal title is entitled to vote unless the rule has been changed by the statute or contract,[5] and even when this is the case an exception is usually made in the case of executors, administrators and trustees.[6] A pledgee, in whose name the stock stands on the books of the corporation, is entitled to vote the shares, unless the right has been reserved by the pledgor.[7] In such case the pledgee holds the legal title, and in the absence of an agreement to the contrary, the right to vote follows the legal title. As between pledgor and pledgee, the pledgor is entitled to exercise the voting power until the title of the pledgee is perfected;[8] and if the stock stands in the name of

325. The stock books, when identified, are competent evidence to show, prima facie, who are shareholders. Turnbull v. Payson, 95 U. S. 418; Hoagland v. Bell, 36 Barb. (N. Y.) 67; Vandermerker v. Glenn, 85 Va. 9; Liggett v. Glenn, 2 C. C. A. 285; Glenn v. Liggett, 47 Fed. Rep. 472; In re St. Lawrence, etc., Co., 44 N. J. L. 529. In Carey v. Williams, 79 Fed. Rep. 906, it was held that the corporation books were not admissible for this purpose. See § 348, *supra*. A stock subscription list, the signatures of which are shown to be genuine, is sufficient proof in the absence of rebutting evidence. Glenn v. Liggett, 47 Fed. Rep. 472.

[1] Brewster v. Hartley, 37 Cal. 15, 99 Am. Dec. 237.

[2] Miller v. Ratterman, 47 Ohio St. 141, 24 N. E. Rep. 496.

[3] State v. Hunton, 28 Vt. 594.

[4] Mack v. DeBardeleben, etc., Co., 90 Ala. 396, 9 L. R. A. 650; State v. Hunton, 28 Vt. 594.

[5] See, where the holder was a mere stockholder, Clarke v. Central, etc., R. Co., 50 Fed. Rep. 338; Commonwealth v. Dalzell, 152 Pa. St. 217, 34 Am. St. Rep. 640; Miller v. Murray, 17 Colo. 408. A prima facie right to vote does not exist until the stock is registered in the name of the person seeking to vote it. Reynolds v. Bridenthal (Neb.), 77 N. W. Rep. 658.

[6] See Hoppin v. Buffum, 9 R. I. 513; Commonwealth v. Dalzell, 152 Pa. St. 217, 34 Am. St. Rep. 640; Brewster v. Hartley, 37 Cal. 15, 99 Am. Dec. 237; In re Barker, 6 Wend. 509.

[7] Commonwealth v. Dalzell, 152 Pa. St. 217, 34 Am. St. Rep. 640; In re Argus, etc., Co., 1 N. D. 434, 26 Am. Rep. 639. Under the Colorado statute the owner of pledged shares may vote the shares. Miller v. Murray, 17 Colo. 408.

[8] Hoppin v. Buffum, 9 R. I. 513;

the pledgee on the books of the corporation, the pledgor may, by a suit in equity, compel the pledgee either to transfer the shares to him, or to give him a proxy. But this right can not be exercised for the purpose of changing the results of the election after the shares have been voted by the pledgee.[1]

Where the stock is held jointly, as by three executors, it can not be voted unless all agree upon the vote.[2] In California it is held that one in whose name shares stand on the books as a trustee can not vote them if he has no actual interest in them.[3] One who held stock as a mere dummy for the owner, for the purpose of avoiding statutory liability, was held not a bona fide holder within the meaning of a statutory provision, and therefore not entitled to vote the stock.[4] The shares held by an estate may be voted by the executors without a transfer to them on the books of the corporation.[5] Stock held by or for the corporation can not be voted either directly or through a trustee.[6] When one corporation has power to hold the stock of another it may vote its stock in the same manner as an individual stockholder.[7] But "in the absence of legislative authority or sanction for such a course of proceeding it is against public

Merchants' Bank v. Cook, 4 Pick. 405. In State v. Smith, 15 Ore. 98, it was held that the pledgee who had secured a transfer to himself of the stock on the books of the corporation, under the authority of the express language of the assignment of the stock, empowering the pledgee to transfer the stock to his own name upon the books, was nevertheless not entitled to vote the stock. The court held that the power to make the transfer on the books, although unlimited and without condition as to time when it might be exercised, could not lawfully be exercised until the pledgee had destroyed the equity of the pledgor by foreclosure. This decision is clearly opposed to that of the court in Nicollet, etc., Bank v. City Bank, 38 Minn. 85, 8 Am. St. Rep. 643, where the court affirms the judgment against defendant for conversion of the stock, because it had refused to transfer the same on its corporate books to the name of the pledgee before the foreclosure of the pledge, while still a mere pledgee.

[1] Hoppin v. Buffum, 9 R. I. 513.

[2] Tunis v. Hestonville, etc., R. Co., 149 Pa. St. 70.

[3] Stewart v. Mahoney, etc., Co., 54 Cal. 149.

[4] Smith v. San Francisco, etc., R. Co., 115 Cal. 584, 35 L. R. A. 309.

[5] Market St. R. Co. v. Hellman, 109 Cal. 571.

[6] American, etc., R. Co. v. Haven, 101 Mass. 398; Ex parte Holmes, 5 Cowen (N. Y.) 426; M'Neely v. Woodruff, 13 N. J. L. 352.

[7] Davis v. United States, etc., Co., 77 Md. 35.

policy to allow one corporation to purchase a majority of the shares in another for the purpose of absorbing it, controlling it, and effecting an unlawful consolidation with it, and a court of equity, having jurisdiction in the premises, will restrain the purchasing corporation from voting at an election in respect of such shares."[1]

§ 472. **Right of bondholders to vote.**—When the law confers the voting power upon the stockholders, the corporation can not, by a contract and by-law, confer it upon the bondholders. Thus, where the constitution of the state conferred the power to elect directors upon the stockholders, it was held that a by-law which also gave the right to the holders of the bonds of the corporation was invalid. The by-law was adopted in pursuance of a contract entered into between the corporation and certain individuals who sold a railroad to the corporation and took the bonds and stock of the company in payment. "The provision made by the corporation, and contained in the bonds and mortgage, that the holders of bonds might vote at any and every meeting of stockholders, is subject to the same objections as the by-laws. Being in violation of express statutory and constitutional provisions, the agreement was inoperative and void. Nor has such provision become binding by subsequent ratification, acquiescence or estoppel. * * * A contract which the corporation could not make, it could not ratify or make valid by any subsequent act. If there was no power to make it there would be equally a lack of power to confer it."[2]

§ 473. **Voting by proxy.**—At common law all votes must be given in person.[3] There is no right to vote by proxy unless it is conferred by statute, charter, or by-law.[4] An invariable usage

[1] Thompson Corps., § 3873. Memphis, etc., R. Co. v. Woods, 88 Ala. 630, 16. Am. St. Rep. 81, 7 L. R. A. 605; Clarke v. Central, etc., R. Co., 50 Fed. Rep. 338, 15 L. R. A. 683. See § 190, *supra*. As between the transferer and the transferee there may be special circumstances which will enable the transferee to vote the stock, although it is not transferred on the books. The corporation, for whose benefit the requirement of registry exists, can not refuse to recognize the transferee after it wrongfully refuses to permit a transfer. Robinson v. Bank, 95 N. Y. 641; Isham v. Buckingham, 49 N. Y. 222.

[2] Durkee v. People, 155 Ill. 355, 46 Am. St. Rep. 340.

[3] Taylor v. Griswold, 14 N. J. L. 222, 27 Am. Dec. 33.

[4] Commonwealth v. Bringhurst, 103

of a corporation to permit voting by proxy is as authoritative as a by-law.[1] General power to enact by-laws includes the power to authorize voting by proxy.[2] No particular form is necessary.[3] The proxy need not be acknowledged or witnessed.[4] It need not state the day of election.[5] The blank of the day and hour of the meeting in proxies sent by a stockholder to the secretary may be filled in by the secretary after their execution.[6] The general rule is that a stockholder can not give an irrevocable proxy,[7] even for a valuable consideration,[8] although it has been held that he may transfer the legal title to a trustee for the purpose of voting, as the transfer is presumably revocable at the will of the beneficial owner.[9] "Irrevocable proxies," not coupled with an interest, according to this view, are revocable, but not necessarily void.[10]

A right to vote by proxy can only be given by the legal

Pa. St. 134, 49 Am. Rep. 119; Craig v. First Presbyterian Church, 88 Pa. St. 42; Taylor v. Griswold, 14 N. J. L. 222; Harben v. Phillips, L. R. 23 Ch. Div. 14; In re St. Lawrence, etc., Co., 44 N. J. L. 529; Market St. R. Co. v. Hellman, 109 Cal. 571; Commonwealth v. Detwiler, 131 Pa. St. 614; People v. Crossley, 69 Ill. 195; State v. Tudor, 5 Day 329; Phillips v. Wickham, 1 Paige Ch. (N. Y.) 590; Perry v. Tuskaloosa, etc., Co., 93 Ala. 364. See note to 27 Am. Dec. 60.

[1] Archer v. Murphy, 26 Wash. L. Rep. 98. Same principle, see Bank v. Pinson, 58 Miss. 421, 38 Am. Rep 330; Miller v. Esbach, 43 Md. 1.

[2] Archer v. Murphy, 26 Wash. L. Rep. 98.

[3] "A stockholder who desires to exercise his right to vote on his stock by proxy is undoubtedly bound to furnish his agent with such written evidence of the latter's right to act for him as will reasonably insure inspectors that the agent is acting by the authority of his principal, but the power of attorney need not be in any prescribed form, nor be executed with any peculiar formality. It is sufficient that it appears on its face to confer the requisite authority, and that it be free from reasonable grounds of suspicion of its genuineness and authenticity; and the court in reviewing the proceedings at an election must be satisfied that the inspectors had reasonable grounds for rejecting the proxy." In re St. Lawrence, etc., Co., 44 N. J. L. 529; Maria v. Garrison, 13 Abb. New Cas. (N. Y.) 210.

[4] In re Cecil, 36 How. Pr. (N.Y.) 477.

[5] In re Townsend, 18 N. Y. Supp. 905.

[6] Ernest v. Loma, etc., Co., 75 Law T. Rep. N. S. 317.

[7] See § 475; Woodruff v. Dubuque, etc., R. Co., 30 Fed. Rep. 91; Griffith v. Jewett, 15 Week. L. B. 419; In re Director Germicide Co., 55 Hun 606.

[8] Reed v. Bank of Newburgh, 6 Paige (N. Y.) 337.

[9] State v. Ohio, etc., R. Co., 6 Ohio C. C. 415. See next section.

[10] Brown v. Pacific, etc., Co., 5 Blatch. (C. C.) 525; Woodruff v. Dubuque, etc., R. Co., 30 Fed. Rep. 91. See Gage v. Fisher, 5 N. Dak. 297, 65 N. W. Rep. 809.

owner of the shares, and in the manner authorized by the charter or by-law. Under authority to give a proxy to "a citizen of the United States," a valid proxy can not be given to an alien.[1] After the death of a stockholder, a proxy must be given by his executors. It can not be given by will, nor are the executors bound to observe a provision in the will that a proxy shall be given by them to a certain person.[2] A sale of the stock will revoke the authority given a third person to vote the stock at a stockholders' meeting.[3] Under a statute which authorizes voting by proxy, a by-law providing that no proxy shall be voted by any one who is not a stockholder of the corporation is invalid.[4]

§ 474. **Personal interest of stockholder—Motive governing vote.**—A shareholder has a legal right, at a meeting of the shareholders, to vote for a measure, although he has a personal interest therein distinct from that of the other shareholders. In such a meeting each shareholder represents himself and his own interests solely and does not act as trustee or representative of others.[5] The motives of the stockholder can not, as a general rule, be made the subject of judicial inquiry.[6] He may, therefore, vote upon a proposition to ratify a contract made by the directors for the purchase of property by the corporation from himself.[7] This rule is not changed by the fact that the stockholder owns the majority of the stock. In such a case the stockholder voted the stock in favor of ratifying a contract which he had made with the corporation as a director, and the supreme court of Canada ordered a rescission of the contract.[8] Chief Justice Richie said: "It does seem to me

[1] In re Barker, 6 Wend. (N. Y.) 509.

[2] Tunis v. Railroad Co., 149 Pa. St. 70.

[3] Ryan v. Seaboard, etc., R. Co., 89 Fed. Rep. 397.

[4] Peoples', etc., Bank v. Sup. Court, 104 Cal. 649, 29 L. R. A. 844, 43 Am. St. Rep. 147. A stockholder is not estopped to question the validity of a meeting by the participation of his proxy therein, as the latter is authorized to vote only at a lawful meeting. Mathews v. Columbus Nat. Bank, 79 Fed. Rep. 558.

[5] Gamble v. Water Co., 123 N. Y. 91, 97.

[6] For an exception to this rule, see Memphis, etc., R. Co. v. Woods, 88 Ala. 630, 16 Am. St. Rep. 81. See § 471, *supra*.

[7] Bjorngaard v. Goodhue, etc., Bank 49 Minn. 483.

[8] Beatty v. Transportation Co., 12 Canada S. C. 598.

that fair play and common sense alike dictate that if the transaction and act of the director are to be confirmed, it should be by the impartial, independent and intelligent judgment of the disinterested shareholders, and not by the interested director himself, who should never have departed from his duty." On appeal, the judgment was reversed by the judicial committee of the Privy Council.[1] "The question involved," said the court, "is doubtless novel by its circumstances, and the decision is important in its consequences. It would be very undesirable even to appear to relax the rules relating to dealings between trustees and beneficiaries ; on the other hand, great confusion would be introduced into the affairs of joint stock companies if the circumstances of shareholders voting in that character at general meetings were to be examined, and their votes practically nullified if they also stood in some fiduciary relation to the company. * * * The only unfairness or impropriety which, consistently with the admitted facts, could be suggested, arises out of the fact that the defendant possessed a voting power as a shareholder which enabled him, and those who thought with him, to adopt the by-law, and thereby either to ratify and adopt a voidable contract, or to make a similar contract, which latter seems to have been what was intended. * * * It may be right that, in such cases, the opposing minority should be able, in a suit like this, to challenge the lien action, and to show that it is an improper one, and to be freed from the objection that a suit with such an object can only be maintained by the company itself. But the constitution of the company enabled the defendant to acquire the voting power; there was no limit upon the number of shares which a stockholder might hold, and for every share so held he was entitled to a vote. * * He had a perfect right to acquire further shares, and to exercise his voting power in such a manner as to secure the election of directors whose views upon policy agreed with his own, and to support those views at any shareholders' meeting; the acquisition of the United Empire was a pure question of policy, as to which it might be expected that there would be differences of opinion, and upon which the

[1] L. R. 12 App. Cas. 598.

voice of the majority ought to prevail; to reject the votes of the defendant upon the question of the adoption of the by-law would be to give effect to the views of the minority, and to disregard those of the majority."

Lord Justice Mellish said: "I am of opinion that, although it may be quite true that the shareholders of a company may vote as they please, and for the purpose of their own interests, yet that the majority of shareholders can not sell the assets of the company and keep the consideration."[1] In commenting upon this language, Sir George Jessel said:[2] "A man may be actuated in giving his note by interests entirely adverse to the interest of the company as a whole. He may think it more for his particular interest that a certain course may be taken, which may be, in the opinion of others, very adverse to the interests of the company as a whole, but he can not be restrained from giving his note in what way he pleases because he is influenced by that motive. There is, if I may say so, no obligation on a shareholder of a company to give his vote merely with a view to what other persons may consider the interests of the company at large. He has a right, if he thinks fit, to give his vote for motives or promptings of what he considers his own individual interests."

But a stockholder is not entirely free from obligation to the other stockholders. Thus, a contract between two stockholders and a third person, by which he was to purchase a part of their stock at par, on condition of being elected treasurer of the corporation, with a condition that the stock should be taken back, in case it should be desirable for any reason to dispense with the plaintiff's services as treasurer, was held invalid. The purpose and effect of the contract was to influence the stockholders in the decision of a question affecting the private rights of others, by considerations foreign to these rights. The promisee was placed under direct inducement to disregard his duties to other members of the corporation who had a right to demand his disinterested action in the selection of suitable officers. He was in a relation of trust and confidence, which required him

[1] Menier v. Hoopers, etc., Works, L. R. 9 Ch. App. Cas. 350, 354.

[2] Pender v. Lushington, L. R. 6 Ch. Div. 70, 74.

to look only to the best interests of the whole, uninfluenced by private gain." [1]

§ 475. **Voting trusts and agreements.**—Numerous devices have been tried by those who were in control of a corporation, for the purpose of keeping a present majority united for the future. Some such agreements have been sustained, but the courts have as a rule frowned upon them as having a monopolistic tendency, being in restraint of trade, and against public policy, because severing the voting power from the ownership of the stock. Thus, proxies in form irrevocable have been held revocable at pleasure. The plan of placing the stock in the hands of trustees, with power to hold and vote the same, and issuing to the stockholders certificates specifying the amount of stock deposited and the beneficial interest of the stockholder therein, failed because the courts held that the holders of the certificates could at any time demand the return of the stock to them.[2] Agreements not to sell their stock for a certain time without the consent of the other stockholders, or to purchasers agreeable to the old stockholders, were held illegal because in restraint of trade.[3] "The most effective way," says Cook,[4] "in which the majority of all the stock in a corporation may be pooled or tied up seems to be selling or transferring it to another corporation formed for that purpose. Such corporation may be organized under the laws of many of the states. The objection to this plan is that it enables the directors of the second corporation to sell the stock at any time, and it involves, not merely a temporary pooling of the stock, but a permanent parting with the title and interest in it."

§ 476. **Voting agreements continued.**—By the weight of authority the law does not absolutely forbid the separation of the voting power from the ownership of the stock. Each case must be determined by its own facts and tendencies.[5] In Ala-

[1] Guernsey v. Cook, 120 Mass. 501. See Gage v. Fisher, 5 N. Dak. 297, 31 L. R. A. 557.

[2] Woodruff v. Dubuque, etc., R. Co., 30 Fed. Rep. 91; Hafer v. New York, etc., R. Co., 14 Weekly Law Bul., 68.

[3] Fisher v. Bush, 35 Hun (N. Y.) 641.

[4] Cook Corp. (3d ed.), § 622.

[5] Fisher v. Bush, 35 Hun (N. Y.) 641. See In re Argus Co., 138 N. Y. 557. See an article by Mr. Justice Baldwin in 1 Yale Law Jour. 1.

bama it was held that there was no objection to a contract by which the stockholders irrevocably surrendered their voting power to a trustee for the benefit of the creditors of the corporation.[1] An agreement between several stockholders, whereby the stock is to be placed with a trust company for a period of six months, and not to be sold during that time, is legal when there is no provision depriving the owner of the right to vote on the stock. The contract being made for the purpose of preventing the sacrifice of the stock, was held not void as against public policy, in restraint of trade, or objectionable because suspending the power of alienation.[2] In California it was held that there may legally be a separation of the voting power and the ownership of stock, and that the owners of the majority of stock may lawfully agree to be bound by the will of the majority, in voting the stock. It was agreed that each one would hold his own shares, but that they should be voted for five years in the way to be determined by the majority of the stock included in the agreement.[3] In Ohio, an agreement between stockholders to transfer their stock to a depositary, who should vote it as directed by a committee of the stockholders for the purpose of adjusting differences between the holders of common and preferred shares, was sustained. It was held not to be a voting trust, but merely "a convenient method by means of which distant and widely separated shareholders became enabled indirectly to participate in the control and management of the company, and from which each could recede at any time and demand the return of his stock without violating any term of the agreement. The depositary is a proxy required to vote the stock as directed by the committee." It was, therefore, held that directors elected by the vote of the depositary were legally elected.[4] A number of shareholders may agree to combine for the purpose of controlling a corporate election and

[1] Mobile, etc., R. Co. v. Nicholas, 98 Ala. 92.

[2] Williams v. Montgomery, 148 N. Y. 519. See this case as to test of alienability of personal property.

[3] Smith v. San Francisco, etc., R. Co., 115 Cal. 584, 35 L. R. A. 309.

[4] Ohio, etc., R. Co. v. State, 49 Ohio St. 668.

the election of such officers as they deem for the best interests of the corporation.[1] A majority who are in accord as to the future policy of a corporation which is to be formed, may enter into a valid agreement for its future management and control, if no statutory provisions are violated.[2] But an agreement by a majority of the stockholders who control the board of directors to the effect that the corporation shall be managed by certain persons is invalid.[3] In North Carolina it was held that an agreement by which the shares were to be transferred to trustees, to be voted as directed by a majority of the stockholders for a period of five years, unless the holders of two-thirds of such stock should vote to end the trust, was contrary to public policy and void as against the rights of an assignee of one of the trustees' certificates to have the shares thereby represented issued to him in his own name.[4]

§ 477. **Voting agreements continued.**—In the Alabama case referred to in the previous section,[5] it appeared that the corporation was in the hands of a receiver, and that its total indebtedness was in excess of its assets. An arrangement was made between the creditors and the company whereby the creditors accepted debentures in lieu of their original evidences of debt and the stockholders assigned their stock to a committee of reorganization, which gave to a trust company an irrevocable power of attorney to vote the stock so long as any of the debentures were outstanding.

The shareholders who thus assigned their stock received in exchange new certificates which entitled them to all the privileges of ownership of the shares, except to the voting power which had been granted to the trust company. Several years after this arrangement had been made, one of the stockholders denied the right of the trust company to vote his stock and filed a bill for an injunction. It was held that the agree-

[1] Faulds v. Yates, 57 Ill. 416; Havemyer v. Havemyer, 11 J. & S. 506, 86 N. Y. 618; Beitman v. Steiner Bros., 98 Ala. 241.

[2] King v. Barnes, 109 N. Y. 267.

[3] Wilbur v. Stoepel, 82 Mich. 344, and see Woodruff v. Wentworth, 133 Mass. 309.

[4] Harvey v. Linville, etc., Co., 118 N. C. 693, 32 L. R. A. 265.

[5] Mobile, etc., R. Co. v. Nicholas, 98 Ala. 92.

ment was valid and binding, and the court said that, "if there were no precedents, upon principle we should hold that in determining the validity of an agreement which provides for the vesting of the voting power in a person other than the stockholder, regard should be had to the condition of the parties, the purpose to be accomplished, the consideration of the undertaking, interests which have been surrendered, rights acquired, and the consequences to result. The law does not make contracts for parties, neither will it annul them, except to preserve its own majesty and to conserve the greater interest of the public. * * * The execution of the decrees of foreclosure by a sale of the property, and the prosecution of the admitted claims against the railroad company, would necessarily have transferred the property to other parties and wiped out every vestige of present available interest or right of the stockholder or hope of future profit. The creditors held the vantage ground, and in law their rights and interest were paramount to those of the stockholders. The latter might accept propositions, but were in no condition to dictate terms. These were the circumstances under which the settlement and agreement were made. Stated in short, the compromise and settlement led to the issue of the debentures to the creditors in lieu of their original evidences of debt and a mortgage upon certain property to secure them; a plan for a sinking fund for their benefit, and the right and privilege under an irrevocable power of attorney to vote the stock *until the debentures were paid*. The power of attorney was not in perpetuity or absolute, but only until the debentures were paid, and a fair construction, under the circumstances, required that the voting power should be used fairly and honestly to this end. * * * Good faith on the part of the assenting stockholders, whose interests were thus preserved, and to those who accepted the debentures in lieu of other evidences of debt and securities, and to those who have since purchased them upon the faith of the plan of compromise, demand that the terms of the contract be fulfilled. Tested by any principle of law, legal

or equitable, the agreement was not only valid, but fair, at least, to the corporation and stockholders."

Even where there can not ordinarily be a separation of the ownership of the shares and the voting power, there may be such a division and conflict of interests as to justify it. In one case[1] it appeared that the railway corporation was in great financial difficulties, and the creditors were threatening to begin foreclosure proceedings. This would have been injurious to the rights of all the stockholders, and as a compromise it was agreed that the creditors' securities and the certificates of stock should be placed under the control of a reconstruction board with power to adjust priorities, execute mortgages and issue new certificates of stock. This board was armed with wide discretion, but was to act with the advice and consent of another body known as the "voting trust," which consisted of five persons. This voting trust was to supervise the reconstruction of the company, and when that was accomplished the certificates of stock were to be issued to them in order that they might elect a president and manager of the road. They were to hold the legal title to the stock, which was to be transferable only on their books, but they were to give the persons who surrendered their stock certificates a beneficial interest, devoid of the right to vote the stock. The court said: "Under the statutes of this state, and on general principles, the right to vote on stock can not be separated from the ownership in such sense that the elective franchise shall be in

[1] Shelmerdine v. Welsh, 20 Phila. Rep. 199, Hare, J., 2 Smith's Corp. Cas. 1039. In Vanderbilt v. Bennett, 6 Pa. Co. Ct. Rep. 193, 2 Smith's Corp. Cas. 1029, an agreement by which the shares were vested in certain trustees who were to have perpetual power to vote the same, for the purpose of carrying out the purpose and policies defined in the agreement, was invalid. At the most it was said to be simply a power of attorney or proxy, and revocable at the option of any party to it. In Hafer v. New York, etc., R. Co., 14 Weekly Law Bulletin 68, an agreement of a similar character, by which the stock was placed in the hands of the representative of a rival company, was held invalid, "both on the ground that the power is denied to one corporation thus to acquire control of another, and that the stockholder can not barter away the right to vote upon his stock." See, also, Griffith v. Jewett, 15 Weekly Law Bulletin 419; Moses v. Scott, 84 Ala. 608, 4 So. Rep. 742.

one man, and the entire beneficial interest in another, nor to any extent, unless the circumstances take the case out of the general rule. It matters not that the end is beneficial and the motive good, because it is not always possible to ascertain objects and motives, and if such a severance were permissible it might be abused. The person who votes must consequently be an owner, but it does not follow that he must be the only one. If, for instance, stock is pledged as a collateral, whether the debtor or creditor shall vote depends on the terms on which the pledge is made. The power is, under these circumstances, necessarily, to some extent, severed from the ownership, and the parties may, consequently, determine on which side it shall lie. So much is conceded on each side of this controversy, and the question is, can the debtor and creditor agree to lodge the vote in some one who is to act for both so long as the debt remains and the stock is held as surety for its payment?" The court held that there is no reason that forbids a stockholder to transfer his shares to one man as security for a debt due another, with a stipulation that the holder should have the right to vote, and that the case was not changed by the fact that the intermediary gave the debtor a certificate that the equitable ownership was in him, subject to the payment of the amount due. It further appearing that the trustee had duties to perform, that is, was not a dry trust, the agreement was held valid.

§ 478. **The Shepaug Voting Trust cases.**—In these cases the supreme court of Connecticut held that it was contrary to public policy to allow the shareholders to deprive themselves of the power to vote their shares, and that an irrevocable proxy can not be given permanently or for a definite period to one who has no beneficial interest or title in the shares.[1] The voting power was placed in a committee, and the court said: "The character of this trust, so far as the trust company is concerned, is a dry trust. The trust company has no beneficial interest

[1] The Shepaug Voting Trust Cases, 60 Conn. (Supp.) 553. See Griffith v. Jewett, 15 Weekly Law Bulletin 419.

whatever in the shares of stock which are made the subject of the trust. They have no interest in favor of which they can claim a continuance of the trust, neither has the committee named in the trust any interest which they, as such committee, can set up for the continuance of the trust. * * * It is the policy of our law that an untrammeled power to vote shall be incident to the ownership of the stock, and a contract by which the real owner's power is hampered by a provision therein that he shall vote just as somebody else dictates, is objectionable. I think it is against the policy of our law for a stockholder to contract that his stock shall be voted just as some one who has no beneficial interest or title in or to the stock directs, saving to himself simply the title, the right to dividends, and perhaps the right to cast the vote directed, willing or unwilling, whether it be for his interest, for the interest of other stockholders, or for the interest of the corporation, or otherwise. This I conceive to be against the policy of the law, whether the power so to vote be for five years or for all time. It is the policy of our law that ownership of stock shall control the property and the management of the corporation, and this can not be accomplished, and this good policy is defeated, if stockholders are permitted to surrender all their discretion and will in the important matter of voting, and suffer themselves to be mere passive instruments in the hands of some agent who has no interest in the stock, equitable or legal, and no interest in the general prosperity of the corporation."

§ 479. **Specific enforcement of such contracts.**—A court of equity will not enforce specific performance of a contract by which one person agrees that another shall control his stock without purchasing it, where the sole object is to secure control of the corporation through the use of the stock which the plaintiff is seeking to acquire. Corporate stock comes within the general rule that the specific performance of a contract for the sale of personal property will not be enforced unless under exceptional circumstances.[1]

[1] Eckstein v. Downing, 64 N. H. 248, 9 Atl. Rep. 626; Appeal of Goodwin,

§ 480. **Number of votes by each stockholder.**—At common law each shareholder was entitled to one vote irrespective of the number of shares held, but by statute and custom it is now the rule to allow one vote for each share of stock.[1] In Taylor v. Griswald[2] a by-law which gave each shareholder a vote for each share of stock held by him was held invalid, as contrary to the common law which gives to all members equal rights, and in violation of the charter. The court said: "The charter, if not in terms, yet in its spirit and legal intendment, gives each member the same rights, and, consequently, but one vote, whereas this by-law gives them unequal rights and an unequal number of votes. It makes one a member for one purpose, and another a member for another purpose. It imposes a test or qualification unknown to the charter, by which to determine how many votes a member may give, whether one, five, ten or fifty. In short, a by-law excluding a member from office, or from the right to vote at all, unless he owns five, ten or twenty shares, would not be a more palpable, though it might be a more flagrant, violation of the charter. A man with one share is as much a member as a man with fifty, and it is difficult to perceive any substantial difference between a by-law excluding a member with one share from voting at all, and a by-law reducing his one vote to cipher by giving another member fifty or a hundred votes." But in modern times it is the interest and not the member which votes, and the practice of giving the shareholder a vote for each share he holds has become so well established that it is fair to imply an intention to follow this custom in the absence of any contrary indication.[3] A by-law containing such a provision is, of course, valid.[4]

etc., Co., 117 Pa. 514, 12 Atl. Rep. 736. In Gage v. Fisher, 5 N. Dak. 297, 65 N. W. Rep. 809, this subject is discussed by Chief Justice Corliss with his usual clearness and thoroughness.

[1] Procter, etc., Co. v. Finley, 98 Ky. 405. In some states the number of votes which may be cast by one stockholder is limited by statute. See Mack v. De Bardeleben, etc., Co., 96 Ala. 396, 9 L. R. A. 650; Commonwealth v. Detwiller, 131 Pa. St. 614.

[2] 14 N. J. L. 222 (1834), 27 Am. Dec. 33. See Angell & Ames Corps., 62; Rex v. Ginever, 6 T. R. 732; Rex v. Decant, 1 Str. 536, Harvard Law Rev., Nov., 1888, p. 156.

[3] Morawetz Priv. Corp., § 476*a*.

[4] Commonwealth v. Detwiller, 131

§ 481. **Cumulative voting.**—Under the system of cumulative voting which has been adopted in a number of states the minority stockholders are authorized to cast a greater number of votes for a particular candidate than they would be entitled to under the ordinary method of casting one vote for each share of stock held.[1] This enables the minority to have a representation on the board of directors, and thus to a certain extent limits the control of the majority over the business policy of the corporation. The right does not exist unless conferred by statute.[2] This method of voting can not be forced upon the corporation contrary to the wishes of the majority of stockholders, as it would impair their contractual rights, unless the state has reserved power to alter, amend, or repeal the corporate charter.[3]

§ 482. **The quorum and majority.**—A quorum is such a number of the members of a body as is necessary to transact the business at a meeting thereof.[4] Less than a quorum have power only to meet and adjourn. The statute or by-laws generally provide that a majority of the stocks shall constitute a quorum at a stockholders' meeting, and a majority in

Pa. St. 614, 18 Atl. Rep. 990; Hays v. Commonwealth, 82 Pa. St. 518.

[1] See Wright v. Central, etc., Co., 67 Cal. 532, 8 Pac. Rep. 70, and State v. Pierce, 51 Kan. 241, 29 Pac. Rep. 565, for construction of constitutional provisions.

[2] State v. Greer, 78 Mo. 188; Hays v. Comw., 82 Pa. St. 518; Baker's App., 109 Pa. St. 461; Smith v. Railroad Co., 64 Fed. Rep. 272.

[3] Attorney-General v. Looker, 111 Mich. 498, 69 N. W. Rep. 929; Cross v. Railway Co., 35 W. Va. 174; State v. Stockley, 45 Ohio St. 304; Pierce v. Comw., 104 Pa. St. 150. In Cross v. W. Va., etc., R. Co., 35 W. Va. 174, the court said: "The state constitution and laws authorizing a stockholder to cumulate his votes constitutes no such impairment, for the reason, among others, that the legislature in the last section of the act of incorporation reserves the right to alter and amend, and in the latter part of the first section requires that all the rules, by-laws and regulations shall not be repugnant to any law of the state then in force, or which might be passed under the power reserved. In Hays v. Com., 82 Pa. St. 518, such a mode of voting was held to be within the protection of the constitution of the United States, as within the obligation assumed by grant of the charter. I do not propose to discuss this question. Here the power to alter is reserved, and such mode of voting is not irrepealable or beyond amendment. State v. Miller, 30 N. J. L. 368, 86 Am. Dec. 188 and notes; Murray v. Charleston, 96 U. S. 432; Railroad Co. v. Gaines, 97 U. S. 697."

[4] Citizens', etc., Co. v. Shortwell, 8 Allen (Mass.) 217.

number at a directors' meeting.[1] A majority of a quorum may bind the corporation.[2] A statute which provides for the adoption of a by-law by a "majority of the stockholders" means a majority in interest of the stockholders, and not necessarily a majority in number.[3] Where the charter and by-laws are silent on the subject, the common-law rule is that such of the stockholders as actually assemble at a properly convened meeting, although a minority of the whole number, and representing only a minority of the stock, constitute a quorum for the transaction of business, and may express the corporate will, and the body will be bound by the acts.[4] "There is a distinction," says Chancellor Kent, "between a corporate act to be done by a select and definite body, as by a board of directors, and one to be performed by the constituent members. In the latter case a majority of those who appear may act, but in the former a majority of the definite body must be present, and then a majority of the quorum may decide. This is the general rule on the subject, and if any corporation has a different modification of the expression of the binding will of the corporation, it arises from the special provisions of the act or charter of incorporation."[5]

It has been held that a majority of the stock represented at the meeting must be voted,[6] but the prevailing rule is that those present and not voting are assumed to vote in the affirmative, and that a majority of the legal votes actually cast, al-

[1] Foster v. Mullanphy, etc., Co., 92 Mo. 79; Ellsworth, etc., Co. v. Fannee, 79 Maine 440; Chase v. Tuttle, 55 Conn. 455; Sargent v. Webster, 13 Met. 497. What shall constitue a quorum may be determined by a by-law. A by-law providing that two-thirds of the stock shall be necessary for a quorum may be repealed by a vote *of a majority of the stock*. Richardson v. Union Cong. Society, 58 N. H. 189.

[2] Field v. Field, 9 Wend. (N. Y.) 394.

[3] Weinburg v. Union, etc., R. Co., 55 N. J. Eq. 640.

[4] Morrill v. Little Falls, etc., Co., 53 Minn. 371, 21 L. R. A. 174; Craig v. First Presbyterian Church, 88 Pa. St. 42; Columbia, etc., Co. v. Meier, 39 Mo. 53; Ex parte Willcocks, 7 Cow. 402; Rex v. Varlo, 1 Cowp. 248.

[5] Com., vol. 2, p. 293. See, also, 1 Kyd Corp., p. 401; Ex parte Willcocks, 7 Cowp. (N. Y.) 402; Elliott Pub. Corp., § 257.

[6] Comw. v. Wickersham, 66 Pa. St. 134.

though a minority of the votes present, prevails.[1] When a meeting is duly called and proper notice given, it is not invalidated by the fact that one of the stockholders is *non compos mentis*, or under other legal disability.[2] If the rule were otherwise "the legal incapacity of a stockholder, such as coverture, infancy or insanity, would operate as an effectual obstacle to a valid assembly of any aggregate corporation. The law confers the attribute of individuality on the entire body constituting a corporation, and in which the individuals are merged. When duly assembled, the corporation itself becomes the individual or person whose acts and proceedings the law alone can regard. If, therefore, it is legally called together, the law presumes that the individual members are competent to transact the business."

The phrase, "holding at least one-third of the shares of stock," in a by-law requiring that number for a quorum, refers to the stock issued and not to the stock authorized, at least when less than one-third of the authorized stock has been issued.[3]

It requires at least two to constitute a "meeting." One individual can not hold a meeting, although he is the owner of a majority of the stock.[4] It has been held, however, that where one person owns the entire stock, he may bind the corporation by contract.[5]

§ 483. **Powers of the majority to manage the corporation.**— The majority of a corporation means that portion of the stockholders present at a general meeting who are entitled to control the corporation by their votes.[6] The right of the majority

[1] State v. Chute, 34 Minn. 135; First Parish v. Stearns, 21 Pick. (Mass.) 148.

[2] Stebbins v. Merritt, 10 Cush. (Mass.) 27.

[3] Castner v. Twitchell, etc., Co., 91 Maine 524, distinguishing Ellsworth, etc., Co. v. Faunce, 79 Maine 440.

[4] England v. Dearborn, 141 Mass. 590; Hopkins v. Roseclare, etc., Co., 72 Ill. 373. In Sharpe v. Dawes, 46 L. J. (Q. B.) 104, one stockholder held a meeting, transacted the business, voted himself a vote of thanks and adjourned. See Morrill v. Little Falls, etc., Co., 53 Minn. 371.

[5] Swift v. Smith, 65 Md. 428. But see Button v. Hoffman, 61 Wis. 20.

[6] Morawetz Priv. Corp., § 476. In Chollar, etc., Co. v. Wilson, 66 Cal. 374, the words "majority of share-

to control is implied in the contract of membership, and they have supreme authority within the scope of the corporate powers to direct the policy of the corporation.[1] Every person who becomes a member agrees, by necessary implication, "that he will be bound by all the acts and proceedings within the scope of the powers conferred by the charter, which shall be adopted or sanctioned by vote of the majority of the corporation, duly taken and ascertained according to law."[2]

But this power does not extend to changing the scope and object of the corporation, or, except under exceptional circumstances, to dissolving the corporation before the expiration of the time fixed in the charter.[3] The majority of the stockholders can not exercise powers which are vested in the board of directors by the charter.[4] "The holders of a majority of the stock of a corporation," says Judge Baxter, "may legally control the company's business, prosecute its general policy, make themselves its agents, and take reasonable compensation for their services. But in thus assuming the control, they also take upon themselves the correlative duty of diligence and good faith. They can not lawfully manipulate the company's business in their own interests to the injury of other stockholders.[5]

§ 484. **Rights of the minority.**—While the majority of the stockholders is entitled to control the policy and general business of the corporation, this power must not be used for the purpose of defrauding the minority.[6] In a case where this

holders," as used in a statute, were construed to mean the majority of all persons holding shares, and not the holders of a majority of the stock.

[1] See § 432, *supra*.

[2] Durfee v. Old Colony, etc., R. Co., 5 Allen (Mass.) 230; Alexander v. Searcy, 81 Ga. 536; Meeker v. Winthrop, etc., Co., 17 Fed. Rep. 48, s. c. 109 U. S. 180; Irvin v. Railway Co., 27 Fed. Rep. 626; Dudley v. Kentucky High School 9 Bush (Ky.) 576.

[3] Barton v. Association, 114 Ind. 226, 16 N. E. Rep. 486.

[4] McCullough v. Moss, 5 Denio (N. Y.) 567. The judgment of the directors will not be controlled by the court at the instance of a majority of the stockholders. Wright v. Lee, 2 S. Dak. 596.

[5] Meeker v. Iron Co., 17 Fed. Rep. 48.

[6] See § 431, *supra*; Bjorngaard v. Goodhue, etc., Bank, 49 Minn. 483; Gamble v. Queens, etc., Co., 123 N. Y. 91; Commonwealth v. Cullen, 13 Pa. St. 133; Chicago, etc., Co. v. Yerkes (Ill.), 30 N. E. Rep. 667; Fougeray v.

was attempted the court said:[1] "Plainly, the defendants have assumed to exercise a power belonging to the majority, in order to secure personal profit to themselves, without regard to the interests of the minority. They repudiate the suggestion of fraud, and plant themselves upon their right as a majority to control the corporate interests according to their discretion. They err if they suppose that a court of equity will tolerate a discretion which does not consult the interests of the minority. It can not be denied that minority stockholders are bound hand and foot to the majority in all matters of legitimate administration of the corporate affairs; and the courts are powerless to redress many forms of oppression, practiced upon the minority under a guise of legal sanction, which fall short of actual fraud. This is a consequence of the implied contract of association by which it is agreed in advance that a majority shall bind the whole body as to all transactions within the scope of the corporate powers. But it is also the essence of the contract that the corporate powers shall only be exercised to accomplish the objects for which they were called into existence, and that the majority shall not control these powers to pervert or destroy the original purposes of the corporation."

The minority is entitled to be heard, and the majority can not arbitrarily refuse to hear arguments against the proposition before the meeting.[2] But a court of equity will not re-

Cord (N. J. Ch.), 24 Atl. Rep. 499. See Barr v. Pittsburg, etc., Co., 51 Fed. Rep. 33.

[1] Wallace, J., in Ervin v. Railway Co., 27 Fed. Rep. 625. See, also, Miner v. Belle Isle, etc., Co., 93 Mich. 97, 17 L. R. A. 412; Livingstone v. Lynch, 4 John. Ch. 573; Hutton v. Hotel Co., 2 Drew & Sm. 514; Brewer v. Boston, etc., Co., 104 Mass. 378; Kean v. Johnson, 9 N. J. Eq. 401; Rollins v. Clay, 33 Maine 132; Clearwater v. Meredith, 1 Wall. 25; Clinch v. Financial Corp., L. R. 4 Ch. App. 117. There is no doubt of the power of a court of equity, in case of fraud, abuse of trust, or misappropriation of corporate funds, at the instance of a single shareholder, to grant relief, and compel a restitution; and where the holders of the majority of stock control the directorate, and are themselves the wrongdoers, without any showing that the directors have been requested, or the corporation has refused, to act. Dodge v. Woolsey, 18 How. 331; Pond v. Railway Co., 12 Blatchf. 280; March v. Railway Co., 40 N. H. 548; Allen v. Curtis, 26 Conn. 456; Hersey v. Veazie, 24 Maine 9.

[2] The majority can not exclude minority from the corporate meeting or

strain the contemplated action of the majority unless it clearly appears that it is so much opposed to the true interests of the corporation as to lead to the clear inference that no one so acting could be influenced by an honest desire to advance the interests of the corporation. An attempt by the majority to exercise a power not possessed by it may result in releasing minority stockholders from liability on their stock subscriptions.[1]

§ 485. **Power of majority to wind up the business.**—A corporation can not dissolve itself, and possibly thus defeat the just rights of its creditors, without the consent of the state.[2] But when the business is manifestly a failure, by the weight of authority the majority of the stockholders may authorize the sale of the entire property of the corporation and wind up the business.[3] "It is unquestionably true," says Mr. Justice Givens,[4] "that a private corporation holds its property as a trust fund for the stockholders, and that, when a majority of the stockholders act together, they are in a sense the corporation, and must act with due regard to the rights of the minority. If the majority decide, arbitrarily and without just cause, to sell the property of the corporation to the prejudice of the minority, and thereby compel the winding up of the business of the corporation, it is a fraud upon the minority, and courts of equity will interfere. If, however, just cause exists for selling the property, as when the corporation is insolvent, and the sale is necessary to pay debts, or where, from any cause, the business is a failure and an unprofitable one, and the best interests of all require it, the majority have clearly the power to order the sale, and in such case their acts are not *ultra vires*. Cook says:[5] 'If, however, the corporation is an unprofitable and failing enterprise, then

deprive them of the right to be heard, by delegating the general power of management to a committee. Great West. R. Co. v. Rushout, 5 De G. & Sm. 290.

[1] Gamble v. Water Co., 123 N. Y. 91.

[2] See § 596, *infra*.

[3] Phillips v. Providence, etc., Co. (R. I. 1899), 43 Atl. R. 598, reviewing cases. See article in 19 Nat. Corp. Rep. 35.

[4] Price v. Holcomb (Iowa), 56 N. W. Rep. 407; Sawyer v. Printing Co., 77 Iowa 242. See Barton v. Association, 114 Ind. 226.

[5] Cook Corp., §§ 656, 662, 667.

a sale of all the corporate property, with a view to dissolution, may be made by the majority of the stockholders.' It would be a harsh rule that would permit one stockholder to hold the others to their investment when just cause existed for closing the business of the corporation."[1] The rule applicable in cases of a co-partnership has been held to apply to such a case. "If it were shown to the court," says Lord Cairns, "that the whole substratum of the partnership—the whole of the business which the company was incorporated to carry on—has become impossible, I apprehend the court might, either under the act of parliament or on general principles, order the company to be wound up. But what I am prepared to hold is this: that this court, and the winding-up process of the court, can not be used as the means of invoking a judicial decision as to the probable success or non-success of a company as a commercial speculation."[2]

§ 486. **Power of majority to accept amendments.**—There is some conflict of authority on the question of the right of the majority to accept amendments to the charter which materially change the character of the corporate enterprise. We have already seen that the state can not impose an amendment of this kind on the corporation without its consent unless it has expressly reserved the power to do so,[3] and the question is whether the giving of this consent is fairly within the power conferred upon the majority by the nature of the contract of membership. The rule of the common law is that when a number of persons associate themselves as partners for a business, and time specified by the articles of agreement between them, or become members of a corporation for definite purposes and objects specified in their charter, the objects and business of the corporation can not be changed or abandoned within the specified time, without the consent of all the partners or corporators. One partner or corporator, however small his interest, can prevent it. This general rule is admitted, although by law a majority in either case can control or manage the business, against the

[1] Lauman v. Railroad Co., 30 Pa. St. 42.

[2] See In re Suburban, etc., Co., L. R. 2 Ch. App. 737; Miner v. Belle Isle, etc., Co., 93 Mich. 97.

[3] Section 103, *supra*.

will and interest of the minority, so long as they act honestly, and within the scope of the partnership or corporate business. The principle seems to be unquestioned, although there is some conflict among the decisions which consider the effect of such material changes and departures under direct authority of the legislature. "This rule is founded on principle, the great principle of protecting every man and his property by contracts entered into, a guiding principle in all right legislation, and incorporated into the constitution of the United States and almost every state of the Union, and the rule is not changed because the new business or enterprise proposed is allowed by law, or has been made lawful since the association was formed.'"[1] Many decisions are to the effect that an amendment which effects a radical change in the corporate enterprise will release a stockholder from liability on his contract of sub-

[1] Chancellor Zabriskie in Zabriskie v. Railway Co., 18 N. J. Eq. 178. See, also, Meadow Dam Co. v. Gray, 30 Maine 547; Old Town, etc., R. Co. v. Veazie, 39 Maine 571. The leading case of Natusch v. Irving was decided by Lord Eldon in 1824. It is not contained in the regular reports, but may be found in the appendix to Gow on Partnership, 3d ed. 576, and in Lindley on Partnership, p. 511. There a partnership was formed for life insurance, and after it was entered into an act of parliament made it lawful for such a firm to enter upon the business of marine insurance, which was prohibited to them before. A majority of the partners determined to embark in the business of marine insurance thus made lawful. Lord Eldon held them barred by the contract of co-partnership, unless every partner agreed to alter it. In England this doctrine is rigidly applied to corporations and is recognized in all the cases. And although from the omnipotent power of parliament restrained by no written constitution, it is held that the contract can be changed by act of parliament, yet the court of chancery will enjoin the directors or the corporation, on the application of a single stockholder, from using the common fund to apply to parliament for a change. The doctrine of Natusch v. Irving was adopted in New York by Chancellor Kent in the case of Livingston v. Lynch, 4 Johns. Ch. 573, and in New Jersey in Kean v. Johnson, 9 N. J. Eq. 401. The opinion of Chancellor Bennett in Stevens v. Rutland, etc., R. Co., 29 Vt. 548, contains a very able exposition and application of the rule. See, also, Angel and Ames on Corp., §§ 391, 393, and §§ 536, 539; Lindley on Partnership, 515; Pierce on Railroads, 78. Hartford, etc., R. Co. v. Croswell, 5 Hill (N. Y.) 383; Troy, etc., R. Co. v. Kerr, 17 Barb. (N. Y.) 581; Macedon, etc., Co. v. Lapham, 18 Barb. (N. Y.) 312; Buffalo, etc., R. Co. v. Pottle, 23 Barb. (N. Y.) 21; Banet v. Alton, etc., R. Co., 13 Ill. 504; Graham v. Birkenhead, etc., R. Co., 2 McN. & G. 156.

scription.[1] In some cases it is held that the reserved power to alter and amend a charter will authorize the majority of a corporation to extend its enterprises without the consent of the minority of the stockholders. The rule was first adopted to enable corporations to subscribe for the stock and bonds of corporations engaged in other enterprises that brought business to them, and was then extended to cases where railroads were authorized to build extensions and branch lines. This rule was adopted in New York,[2] but it was said in New Jersey,[3] "That if the change in the act is simply offering the corporation the privilege of entering on another and a different enterprise, it is not within the condition to the subscription. The only construction to be given is that the legislature may alter, not that the stockholders may as between each other. The case of Natusch v. Irving was decided upon this very ground. The act of parliament had given the company power to embark in marine insurance, but the consent of all the parties was still held necessary. The plain object of the reservation in this case was to give the legislature, not a bare majority of the stockholders, power. This view of the case is so clear upon principle that I feel constrained to be guided by it, although the weight of decisions in other states is against it."

§ 487. **Power to accept amendments, continued.**—In a few cases it is held that the majority may accept an amendment offered by the legislature, which authorizes the corporation to enter upon a new and different enterprise. The leading case was an application for an injunction by a minority shareholder to restrain the corporation from constructing an extension to its line of railroad. Chief Justice Bigelow said:[4] "The case for

[1] Ashton v. Burbank, 2 Dill. (C. C.) 435; Union Locks, etc., v. Towne, 1 N. H. 44; Manheim, etc., Co. v. Arndt, 31 Pa. St. 317; Southern, etc., R. Co. v. Stevens, 87 Pa. St. 190; Hartford, etc., R. Co. v. Croswell, 5 Hill (N. Y.) 383.

[2] North, etc., R. Co. v. Miller, 10 Barb. (N. Y.) 260; White v. Syracuse, etc., R. Co., 14 Barb. (N. Y.) 559; Plank Road Co. v. Thatcher, 1 Kern (N. Y.) 102; Buffalo, etc., R. Co., v. Dudley, 4 Kern (N. Y.) 336.

[3] Zabriskie v. Railroad Co., 18 N. J. Eq. 178.

[4] Durfee v. Old Colony, etc., R. Co., 5 Allen (Mass.) 230. See also White v. Railroad Co., 14 Barb. N. Y. 559; Buffalo, etc., R. Co. v. Dudley, 14 N. Y 336, § 432.

the plaintiff mainly rests on the single proposition of law that a corporation established by the legislature of this commonwealth by acts which * * * are subject to alteration, amendment or repeal at the pleasure of the legislature, can not engage in any new enterprise or enter upon any new undertaking in addition to that contemplated by and embraced in the original charter of the company against the consent of any one of its stockholders, although such new enterprise or undertaking is of the same kind with that for which the corporation was originally established, and is authorized, sanctioned and adopted by an express legislative grant and by a vote of the majority of the stockholders duly ascertained according to law. * * * We suppose it may be stated as an indisputable proposition that every person who becomes a member of a corporation aggregated by purchasing and holding shares, agrees, by necessary implication, that he will be bound by all acts and proceedings within the scope of the powers and authority conferred by the charter, which shall be adopted or sanctioned by a vote of the majority of the corporation duly taken and ascertained according to law. This is the unavoidable result of the fundamental principle that the majority of the stockholders can regulate and control the lawful exercise of the powers conferred on a corporation by its charter. The holder of shares in an incorporated body, so far as his individual rights and interests may be involved in the doings of the corporation, acting within the legitimate sphere of its corporate power, has no other legal control over them than that which he can exercise by his single vote in the meetings of the company. * * * When, therefore, it is expressly provided, between the legislature on the one hand and the corporation on the other, as part of the original contract of incorporation, that the former may alter or change or abrogate it or any portion of it, it can not be said that any contract is broken or infringed when the power thus reserved is exercised, with the consent of the artificial body of whose original creation and existence such reservation formed an essential part. * * * If it be asked by whom such amendment or alteration is to be

made, the answer is obvious, by the parties to the contract, the legislature on the one hand and the corporation on the other; the former expressing its intention by means of a legislative act, and the latter assenting thereto by a vote of the majority of the stockholders, according to the provisions of its charter.

§ 488. **Immaterial amendments and alterations.** — An amendment which does not materially change the charter or affect the scope of the corporate enterprise, and thus the contract of membership, may be accepted by the majority acting under legislative authority. Under this rule the difficulty is in determining what are material and fundamental alterations, and no general rule can be laid down.[1] Thus, where an amendment changed the name, increased the capital and extended the road of a plank road and railroad corporation, the court said: "The change is not fundamental. The new powers conferred are identical in kind with those originally given. They are enlarged merely, the general objects and purposes remaining the same. It may be admitted that under this reserved power to alter and repeal, the legislature would have no right to change the fundamental character of the corporation and convert it into a different legal being, for instance, a banking corporation, without absolving those who did not choose to be bound."[2]

The majority can not accept an amendment which authorizes an insurance company organized to transact a "life and accident insurance business," to do "fire, marine and inland insurance." Judge Dillon said:[3] "The change in the charter by which a life and accident company was authorized to transact fire, marine and inland insurance, is an organic

[1] See cases cited by Justice Strong in Nugent v. Supervisors, 19 Wall. (U. S.) 241; Witter v. Miss., etc., R. Co., 20 Ark. 463, 493; Taggart v. Railroad Co., 24 Md. 563; Union, etc., Assn v. Neill, 31 Iowa 95; Union, etc., Co. v. Hersee, 79 N. Y. 454; Rutland, etc., R. Co. v. Thrall, 35 Vt. 536; Everhart v. Railway Co., 28 Pa. St. 339; Banet, v. Alton, etc., R. Co., 13 Ill. 504; Pacific R. Co. v. Renshaw, 18 Mo. 210; Pacific R. Co. v. Hughes, 22 Mo. 291; Howard v. Glenn, 85 Ga. 238.

[2] Buffalo, etc., Co. v. Dudley, 14 N. Y. 336; Schenectady, etc., Co. v. Thatcher, 11 N. Y. 102.

[3] Ashton v. Burbank, 2 Dill. C. C. 435.

change of such a radical character as to discharge previous subscribers to the stock of the company from any obligation to pay their subscription, unless the change is expressly or impliedly assented to by them. Here there was no such assent, and no acquiescence in the structural change made in the charter of the company. The company could not, against such a subscriber, maintain a suit to collect his subscription, and take the money and use it as capital for the transaction of business under the charter as altered. We think in such a case the subscriber is not bound to enjoin action under the amended charter, but may, if he elects, defend against an action to recover on his subscription to the stock. If the company accepted the amended charter, as it did by adopting the new name, it is not essential to such a defense to show that, at the time of the trial, the corporation had actually exercised the enlarged powers conferred upon it. The defendants are not bound on their subscription to pay to the company money which, if paid, may be used as capital to carry on the business authorized by the amended charter."

A subscriber is not released by the acceptance of an amendment to the charter of a railroad corporation authorizing it to build a branch road[1] or slightly altering the route.[2] But a substantial change of the route will discharge the subscriber.[3]

§ 489. **Material beneficial amendments.**—One line of authorities holds that the majority may, against the wishes of the minority, accept an amendment which, although it materially alters the charter, is manifestly beneficial to the corporation, and along the line of the general objects for which it was originally created. The reasons upon which this rule rests are thus stated by the supreme court of Illinois.[4] "An alter-

[1] Peoria, etc., R. Co. v. Preston, 35 Iowa 115.

[2] Wilson v. Valley, etc., R. Co., 33 Ga. 466.

[3] Middlesex, etc., Corp. v. Locke, 8 Mass. 268; Buffalo, etc., R. Co. v. Pottle, 23 Barb. (N. Y.) 21; Moore v. Hanover, etc., R. Co., 94 Pa. St. 324.

[4] Banet v. Alton, etc., R. Co., 13 Ill. 504. See, also, Illinois, etc., R. Co. v. Zimmer, 20 Ill. 654; Pacific R. Co. v. Renshaw, 18 Mo. 210; Hartford, etc., R. Co. v. Croswell, 5 Hill (N. Y.) 383; Gray v. Navigation Co., 2 Watts & S. (Pa.) 156. See comment upon this case in Hartford R. Co. v. Croswell, 5 Hill (N. Y.) 383.

ation in a charter may be so extensive as to work a dissolution of the contract of subscription. An amendment which essentially changes the nature or objects of a corporation will not be binding on the stockholders. A corporation formed for the purpose of constructing a railroad can not be converted into a company to construct an improvement of a different character without the consent of all the corporators. A road intended to secure the advantages of a particular line of travel and transportation can not be so changed as to defeat that general object. The corporation must remain substantially the same, and be designed to accomplish the same general purposes and subserve the same general interests. But such amendments of the charter as may be considered useful to the public and beneficial to the corporation, and which will not divert its property to new and different purposes, may be made without absolving the subscribers from their engagement. The straightening the line of the road, the location of a bridge at a different place on a stream, or a deviation in the route from an intermediate point, will not have the effect to destroy or impair the contract between the corporation and the subscribers. We regard these conclusions as reasonable and just, and as well calculated to facilitate the construction of improvements and promote the best interests of the public and the stockholders. The incidental benefit which a few subscribers may realize from a particular location ought not to interfere with the general interest of the public and the great mass of the corporators. These interests of the public and the majority of the subscribers may with propriety be consulted and encouraged, especially where the alteration will not operate to depreciate the value of stock."

§ 490. **Elections—Presumption of regularity.**—The manner of electing the officers and directors of a corporation is ordinarily regulated by the charter or by-laws or by custom. In the absence of any specific provision, all that is essential to a valid election is that the will of the members be fairly expressed.[1]

[1] In re Chenango Co., etc., Co., 19 etc., 19 Wend. (N. Y.) 135. Wend. (N. Y.) 635· In re Election,

Every presumption is in favor of the validity of the proceedings.[1] Thus it will be presumed that a quorum was present until the contrary appears.[2] So, where the by-laws provide that the stockholders' meeting shall be held at the counting-room of the corporation, and it appeared that it was held at the dwelling-house of the manager, it was presumed that the counting-room was in the dwelling-house.[3]

§ 491. **Inspectors of elections.**—The right to appoint inspectors or judges of election is vested in the shareholders, and not in the board of directors.[4] Such power, however, may be delegated to the directors by a by-law. The legal owner of stock is entitled to vote upon it, and the inspectors have no power to inquire into the question of the equitable ownership,[5] or to assume a judicial power to try the genuineness of a proxy if it is in regular form.[6] The duties are ministerial, and not judicial.[7] The fact that the inspectors are not sworn, or are sworn in an improper manner, will not invalidate an election, if no objection is interposed at the time.[8]

§ 492. **Illegal votes.**—An election is not necessarily rendered void by the reception of illegal votes. Where a candidate at a corporate election receives a majority of the legal votes cast, the receipt of illegal votes in his favor does not defeat his election.[9] Votes for ineligible candidates are generally disregarded or "thrown away." "Votes cast for a candidate who is disqualified for the office will not be thrown away so as to make the election fall on a candidate having a minority of votes, unless the electors casting such votes had knowledge of the facts on which the disqualification of the candidate for

[1] Hathaway v. Addison, 48 Maine 440.

[2] Citizens', etc., Co. v. Sortwell, 8 Allen (Mass.) 217.

[3] McDaniels v. Manufacturing Co., 22 Vt. 274.

[4] State v. Merchant, 37 Ohio St. 251.

[5] See Morawetz Priv. Corp. I, § 484.

[6] Matter of Cecil, 36 How. Pr. (N. Y.) 477.

[7] Comw. v. Woelper, 3 Serg. & R. 29.

[8] In re Election of Directors, etc., 19 Wend. (N. Y.) 135.

[9] In re Argus Co., 138 N. Y. 557; First Parish v. Stearns, 21 Pick. (Mass.) 148; In re Chenango, etc., Co., 19 Wend. (N. Y.) 635; Ex parte Murray, 7 Cowen (N. Y.) 153.

whom they voted rested, and also knew that the latter was for that reason disqualified from holding office.'"[1] It has been held that votes improperly cast should be disregarded by the court.[2] The objection that illegal votes were cast at an election must be made at the time they are offered.[3] If there are no inspectors of election, the meeting itself must determine who are entitled to vote, as the presiding officer has no such power. A person who refrains from voting because the presiding officer rules that he is not entitled to vote can not afterwards be heard to complain, as he should have appealed from the decision to the meeting.[4] He must show that he properly presented his claim to vote, and that it was rejected by the proper authority.

§ 493. **Control of courts over corporate elections.**—If the proper officers of a corporation fail or refuse to call a meeting for the election of officers or directors at a proper time, they may be compelled to do so at the instance of a stockholder.[5] A court of law is the proper tribunal to try the validity of a corporate election, and it is generally held that a court of equity has no jurisdiction, unless it is specially conferred upon it by statute,[6] or the question arises in the determination of a suit which is properly cognizable by a court of equity.[7] An injunction will issue on the application of the real owner of the stock to restrain the voting of stock under a pooling arrangement which is against public policy.[8] So it has been held that by an injunction a stockholder may obtain the cancellation of illegal shares, and restrain the holders from vot-

[1] In re St. Lawrence, etc., Co., 44 N. J. Law 529. See Horton v. Wilder, 48 Kan. 222; Thompson Corp., § 752.

[2] Baker's App., 109 Pa. St. 461.

[3] In re Chenango, etc., Co., 19 Wend. (N. Y.) 635.

[4] State v. Chute, 34 Minn. 135. See 19 Wend. 37; 1 Denio 388, 396; 1 Wend. 98.

[5] People v. Cummings, 72 N. Y. 433; State v. Wright, 10 Nev. 167.

[6] Mechanics, etc., Bank v. Burnet, etc., Co., 32 N. J. Eq. 236; Kean v. Union, etc., Co., 52 N. J. Eq. 813; Neall v. Hill, 16 Cal. 145. A method for reviewing corporate elections is often provided by statute. See Re Newcomb, 42 N. Y. St. 442; Wickersham v. Brittan, 93 Cal. 34, 15 L. R. A. 106.

[7] As to the limitations, see New England, etc., Co. v. Phillips, 141 Mass. 535.

[8] Harvey v. Linville, etc., Co., 118 N. C. 693, 32 L. R. A. 265.

ing such shares.[1] So a stockholder may restrain the voting of stock in a manner contrary to the charter of the corporation.[2] The prevailing view seems to be that a court of equity has no superintendence over corporate elections, although it is said to possess an imperfect jurisdiction, and the tendency is to extend this and to hold that when necessary in order to secure a fair and honest election, it may appoint a master to conduct the same.[3] A proceeding to set aside an election of officers, because not made in conformity to the law, may be brought by one who has not been a stockholder long enough to entitle him to vote under the rules of the corporation.[4]

[1] Wood v. Church, etc., Assn., 63 Wis. 9.

[2] Webb v. Ridgely, 38 Md. 364.

[3] Tunis v. Railway Co., 149 Pa. St. 70; Wright v. Central, etc., R. Co., 67 Cal. 532. See Thompson's Corps., §§ 3877, 3878, and cases there cited.

[4] Wright v. Central, etc., R. Co., 67 Cal. 532. The ordinary method by which to try the title to an office is an information in the nature of a *quo warranto*. See Elliott Pub. Corp. § 349; State v. Sullivan, 45 Minn. 309, 11 L. R. A. 272; State v. Bulkeley, 61 Conn. 287, 14 L. R. A. 657; People v. Londoner, 13 Colo. 303, 6 L. R. A. 444.

CHAPTER 18.

OFFICERS AND AGENTS AND THE MANAGEMENT OF CORPORATIONS.

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§ 494. **General statement.**—A corporation must necessarily act through agents, and the relation between directors and

other officers and the corporation is that of principal and agent. Such officers in their dealings with the corporation are governed by the general principles of the law of agency.[1] The charter commonly provides that the management of the corporation shall be by certain specified agents, but this is implied in the absence of such provision.[2] No formalities are required in the appointment of agents unless provided for by charter,[3] and a corporation may be bound by acquiescence in the acts of a person who assumes the authority of an agent, but who in fact was never authorized to act for the corporation.[4]

§ 495. **Presumption of authority.**—In a recent case[5] the following language of Judge Thompson was quoted with approval: "A very extensive principle in the law of corporations, applicable to every kind of written contract executed ostensibly by the corporation, and to every kind of act done by its officers in its behalf, is that where the officer or agent is the appropriate officer or agent to execute a contract, or to do an act of a particular kind in behalf of the corporation, the law presumes a precedent authorization regularly and rightfully made; and it is not necessary to produce evidence of such authority from the records of the corporation. Under the operation of this principle a deed or mortgage purporting to have been executed by a corporation, which is signed and executed in its behalf by its president and secretary, will be presumed to have been executed by its authority."[6] This rule is of general application.[7]

[1] Wayne, etc., Co. v. Hammons (Md.), 27 N. E. Rep. 487; Port v. Russell, 36 Ind. 60.

[2] Protection, etc., Co. v. Foote, 79 Ill. 361; Hurlbut v. Marshall, 62 Wis. 590.

[3] Bank v. Dandridge, 12 Wheat. (U. S.) 64; Sherman v. Fitch, 98 Mass. 59; Roberts v. Deming, etc., Co., 111 N. Car. 432.

[4] Goodwin v. Union, etc., Co., 34 N. H. 378.

[5] Ellison v. Brandstrater (Ind.), 54 N. E. Rep. 433.

[6] Thompson Corps., §§ 5029, 5730.

[7] National Bank v. Vigo Nat. Bank, 141 Ind. 352; National, etc., Co. v. Rockland Co., 94 Fed. Rep. 335; Gorder v. Plattsmouth, etc., Co., 36 Neb. 548; Merchants, etc., Bank v. Citizens, etc., Co., 159 Mass. 505; New England, etc., Co. v. Farmington, etc., Co., 84 Me. 284; Steel Works v. Bresnahan, 60 Mich. 332; City of Lincoln v. Sun,

§ 496. **The general management—Directors—Directors' meetings.**—The general management of the corporation is vested in the board of directors as a board, and not in the individual members thereof, and they have no authority to act save when assembled at a board meeting. The separate action, individually, of the persons composing such governing body is not the action of the constituted body clothed with corporate powers.[1] But a director may be appointed by the board to act as their agent.[2] Directors continue to hold office until their successors are elected and qualified.[3] The directors have no implied power to fill vacancies in their number.[4] The governing body of the corporation can be compelled by mandamus to order an election to choose a board of directors.[5] Notice of a directors' meeting must be given in the same manner as notice of a shareholders' meeting.[6] But when all the directors are

etc., Co., 59 Fed. Rep. 756, 8 C. C. A. 253; Malone v. Trans. Co., 77 Cal. 38; Devlin on Deeds, § 343 and note. An act done by the president of a corporation pertaining to its business, not clearly foreign to his power, will be presumed to have been authorized. Anderson v. South, etc., Co., 173 Ill. 213.

[1] Baldwin v. Canfield, 26 Minn. 43; Calumet, etc., Co. v. Haskell, etc., Co., 144 Mo. 331, 66 Am. St. Rep. 425; Titus & Scudder v. Cairo, etc., R. Co., 37 N. J. L. 98; Buttrick v. Railroad Co., 62 N. H. 413; Bank v. Christopher, 40 N. J. L. 435; Hillyer v. Min. Co., 6 Nev. 51; Filon v. Brewing Co., 38 N. Y. St. 602. But see Bank v. Rutland, etc., R. Co., 30 Vt. 159; Longmont, etc., Co. v. Coffman, 11 Colo. 551. Resolutions of a corporation passed at an irregular, unlawful special meeting of the directors are not admissible in evidence against the corporation in support of notes which they attempt to authorize. Pauly v. Pauly, 107 Cal. 8, 48 Am. St. Rep. 98.

[2] Northampton Bank v. Pepoon, 11 Mass. 288.

[3] As to what amounts to a resignation of a director, see Chemical, etc., Bank v. Colwell, 132 N. Y. 250; Berry v. Cross, 3 Sandf. Ch. (N. Y.) 1; Briggs v. Spaulding, 141 U. S. 132.

[4] Moses v. Tompkins, 84 Ala. 613.

[5] People v. Cummings, 72 N. Y. 433.

[6] § 467 *supra;* Thompson v. Williams, 76 Cal. 153, 9 Am. St. Rep. 187; Herrington v. Liston, 47 Iowa 11. As to necessity of notice to a director to attend a special meeting, see note to 3 Am. St. Rep. 69–70. American, etc., Bank v. First Nat'l Bank, 82 Fed. Rep. 961, 48 U. S. App. 633. It has been held, under a charter which provided that a specified number of directors should constitute a quorum, that if a quorum is present it is immaterial that notice of the meeting was not given the others. Edgerly v. Emerson, 23 N. H. 555; Bank v. Flour Co., 41 Ohio St. 552; State v. Smith, 48 Vt. 266; Chase v. Tuttle, 55 Conn. 455.

present or participate in a meeting, the fact that no notice was given is immaterial.[1] The time of regular meetings may be fixed by the charter, by-laws or by usage.[2] The ordinary business of the board may be transacted under a general notice. When no particular purpose or object is stated in the notice, it is presumed that the meeting was called for the consideration of all matters relating to the ordinary business of the corporation that may come before it.[3] In the absence of evidence to the contrary it will be presumed that proper notice of the meeting was given to all directors.[4] A majority of the whole number of directors is necessary to constitute a quorum in the absence of an express provision for a lesser number. A majority of the quorum may bind the corporation.[5] But, in order that a quorum may act for the corporation, it is necessary that all the directors should have had notice of the meeting, unless the charter expressly provides that a designated number of directors shall constitute a quorum.[6] A majority of the quorum must be disinterested in respect to matters voted upon.[7]

§ 497. **Place of directors' meetings.**—Stockholders' meetings are generally required to be held in the state where the corporation was created, but the authorities are now uniform that an agent of a corporation may exercise its powers out of the state incorporating it providing there is nothing in its charter or in the nature of its affairs contravening it. If one agent may thus act there would seem to be no sensible reason why a board of directors may not do so, and as directors are only

[1] Minneapolis, etc., Co. v. Nimocks, 53 Minn. 381; Troy, etc., Co. v. White, 10 S. Dak. 475.

[2] Atlantic, etc., Co. v. Sanders, 36 N. H. 252-269.

[3] In re Argus Co., 138 N. Y. 557. See Chase v. Tuttle, 55 Conn. 455, 3 Am. St. Rep. 64.

[4] Chase v. Tuttle, 55 Conn. 455.

[5] Ten Eyck v. Pontiac, etc., R. Co., 74 Mich. 226, 16 Am. St. Rep. 633; Sargent v. Webster, 13 Mete. (Mass.) 497; Leavitt v. Mining Co., 3 Utah 265. A majority of the quorum is essential to the adoption of a resolution. Smith v. Los Angeles, etc., Assn., 78 Cal. 289, 12 Am. St. Rep. 53.

[6] Edgerly v. Emerson, 23 N. H. 555; Chase v. Tuttle, 55 Conn. 455. The presumption is in favor of the regularity of the meeting. Heintzelman v. Association, 38 Minn. 138; Dispatch v. Bellamy, etc., Co., 12 N. H. 205; Thompson v. Williams, 76 Cal. 153, 9 Am. St. Rep. 187.

[7] Miner v. Ice Co., 93 Mich. 97; Smith v. Association, 78 Cal. 289.

agents the principle is broad enough to include them.[1] The principal office of a corporation is the place where its stockholders and directors usually meet, and where it elects its officers and transacts its financial business.[2]

§ 498. **Qualifications of directors.**—A director is merely an agent, and any person who has capacity to contract may be a director of a corporation. No special qualifications are necessary unless required by the charter or by-laws.[3] A director need not be a shareholder unless required to be such by the charter, or, as is commonly the case, by statute.[4] Where a director is required to be a shareholder, it is sufficient if the shares stand in his name on the books of the corporation.[5] But it has been held that when a director is required to be a stockholder, he must be the beneficial owner, and that the

[1] Wood, etc., Co. v. King, 45 Ga. 34. See § 465, *supra*; Wright v. Lee, 2 S. Dak. 596, 51 N. W. Rep. 706; Arms v. Conant, 36 Vt. 744; Saltmarsh v. Spaulding, 147 Mass. 224; Bellows v. Todd, 39 Iowa 209; McCall v. Manufacturing Co., 6 Conn. 428. See, as to stockholders' meetings, Hodgson v. Duluth, etc., R. Co., 46 Minn. 454.

[2] Frick Co. v. Norfolk Bank, 86 Fed. Rep. 725; 57 U. S. App. 286. See also, Jossey v. Georgia R. Co., 102 Ga. 706. It may be implied and established from the acts of the stockholders and directors. Frick v. Norfolk Bank, *supra;* Dade, etc., Co. v. Haslett, 83 Ga. 549. The office of the president will be presumed to be the proper place of holding meetings. Troy, etc., Co. v. White, 10 S. Dak. 475.

[3] The treasurer may be a director. Sargent v. Webster, 13 Met. (Mass.) 497, 46 Am. Dec. 743. An alien residing in the state may be a director. Commonwealth v. Hemmingway, 131 Pa. St. 614. A non-resident may be a director. See State v. Smith, 15 Ore. 98, and Horton v. Wilder, 48 Kan. 222. A corporation may, by a by-law, provide that no one who is an attorney in a suit against the corporation shall be eligible as a director. Cross v. West Va., etc., R. Co., 37 W. Va. 342, 18 L. R. A. 582.

[4] Wright v. Springfield, etc., R. Co., 117 Mass. 226, 19 Am. Rep. 412; People v. Northern R. Co., 42 N. Y. 217. One who acts as a director will be treated as one in a controversy between himself and the corporation, although he is not a stockholder. Stetson v. Northern, etc., Co., 104 Iowa 393. A member of an assessment fire insurance company only can fill the office of director. State v. Manufacturers', etc., Assn., 50 Ohio St. 145, 24 L. R. A. 252.

[5] Re Argus, etc., Co., 1 N. Dak. 434, 26 Am. St. Rep. 639; State v. Leete, 16 Nev. 242. *Compare* State v. Hunton, 28 Vt. 594; Chase v. Tuttle, 55 Conn. 455, 3 Am. St. Rep. 64.

mere fact that shares are registered in his name is not sufficient.[1] A by-law which provides that a director shall cease to be such when he ceases to be a proprietor of shares, by implication, renders one who is not the proprietor of shares ineligible to the office of director.[2] A bona fide owner of shares is eligible, although they have not been transferred to him on the books.[3] A director who is required to be a stockholder divests himself of his office by disposing of his stock.[4] A director's qualification shares may be held by him jointly with another person.[5]

§ 499. **Powers of directors.**—The board of directors has implied power to do whatever the corporation may lawfully do in the transaction of its ordinary business. For the purpose of dealing with others it is the corporation.[6] But the authority "extends merely to the supervision and management of the company's ordinary and regular business." The directors have no implied authority to make a permanent and material alteration of the business or constitution of the corporation, although the business as so altered is within the company's chartered powers.[7] Thus, they can neither increase the capital stock,[8] nor lease the entire property of the corporation,[9] nor sell the property and wind up the business of the corporation.[10]

[1] Brainbridge v. Smith, L. R. 41 Ch. Div. 462, 33 Am. and Eng Corp. Cas. 172 (annotated), Lindley, L. J., dissenting, overruling the decision of Sir George Jessel, M. R., in Pulbrook v. Richmond, etc., Co., L. R. 9 Ch. Div. 610.

[2] Dispatch Line v. Bellamy, etc., Co., 12 N. H. 205, 37 Am. Dec. 203.

[3] State v. Smith, 15 Ore. 98, 14 Pac. Rep. 814, 15 Pac. Rep. 137.

[4] Chemical Nat. Bank v. Colwell, 132 N. Y. 250.

[5] In re Glory, etc., Co., L. R. (1894) 3 Ch. 473.

[6] Burrill v. Nahant Bank, 2 Met. (Mass.) 163; Hoyle v. Railway Co., 54 N. Y. 314; Reichwald v. Commercial, etc., Co., 106 Ill. 439; Eastern R. Co. v. Railway Co., 111 Mass. 125; Leavitt v. Oxford, etc., Co., 3 Utah 265; Bliss v. Kaweah, etc., Co., 65 Cal. 502; Donohoe v. Mariposa, etc., Co., 66 Cal. 317; Heintzelman v. Druids', etc., Assn., 38 Minn. 138. The power to ratify the unauthorized acts of agents is presumed to be in the board of directors. Western, etc., Assn. v. Ready, 24 Minn. 350.

[7] Morawetz Priv. Corp. I, § 512; Railway Co. v. Allerton, 18 Wall. 233.

[8] Railway Co. v. Allerton, 18 Wall. 233; Eidman v. Bowman, 58 Ill. 444.

[9] Martin v. Railway Co., 14 Phila. 10.

[10] Rollins v. Clay, 33 Maine 132.

But by the weight of authority they may transfer its property to an assignee for the benefit of creditors when the condition of its affairs is such as to reasonably justify such a course.[1] The directors have no power to admit in writing the inability of the corporation to pay its debts as the basis of an involuntary petition in bankruptcy. Such an act is not binding upon the corporation.[2]

§ 500. **Stockholders' control over directors.**—The power of management vested in the board of directors is conclusive in its character. Their will must govern in the absence of fraud or breach of trust, and the courts will not, even on the petition of the majority of the stockholders, compel the directors to do an act contrary to their judgment.[3]

§ 501. **Delegation of authority—Executive committee.**—The board of directors of a corporation may delegate the ordinary routine business,[4] such as the appointment of an agent to execute a deed[5] or a note,[6] to subordinate agents. Some authorities hold that matters involving discretion can not be delegated,[7] but by the weight of authority a board of directors may delegate its powers to an executive committee,[8] and the majority of this committee constitutes a quorum which can bind the corporation by its acts.[9]

[1] § 189, Tripp v. N. W. Nat'l Bank, 41 Minn. 400; Dana v. Bank of the U. S., 5 Watts & S. 223; Ardesco, etc., Co. v. North Am., etc., Co., 66 Pa. St. 375; DeCamp v. Alward, 52 Ind. 468; Chamberlain v. Bromberg, 83 Ala. 576; Chase v. Tuttle, 55 Conn. 455; Wilkinson v. Bauerle, 41 N. J. Eq. 635.

[2] Re Bates, etc., Co., 91 Fed. Rep. 625.

[3] Dodge v. Woolsey, 18 How (U. S.) 331; Hunter v. Roberts, etc., Co., 83 Mich. 63, 47 N. W. Rep. 131; Sims v. St. R. Co., 37 Ohio St. 556; Moses v. Thompkins, 84 Ala. 613; Pratt v. Pratt, Read & Co., 33 Conn. 446.

[4] Manchester, etc., R. Co. v. Fisk, 33 N. H. 297.

[5] Arms v. Conant, 36 Vt. 744.

[6] Leavitt v. Oxford, etc., Co., 3 Utah 265.

[7] Weidenfeld v. Sugar, etc., R. Co., 48 Fed. Rep. 615; Gillis v. Bailey, 21 N. H. 149; Temple v. Dodge, 89 Texas 68.

[8] Sheridan, etc., Co. v. Chatham, etc., Bank, 127 N.Y. 517; Union, etc., R. Co. v. Chicago, etc., R. Co., 163 U. S. 564, 597; Union, etc., R. Co. v. Chicago, etc., R. Co., 51 Fed. Rep. 309; Black River, etc., Co. v. Holway, 85 Wis. 344.

[9] Burleigh v. Ford, 61 N. H. 360. As to powers of an auditing committee,

§ 502. **Relation of officers and directors to the corporation.** —The officers and directors of a corporation are variously referred to as agents, trustees or mandatories.[1] Judge Sharswood says:[2] "It is by no means a well settled point what is the precise relation which directors sustain to stockholders. They are undoubtedly said in some authorities to be trustees; but that, as I apprehend, is only in a general sense, as we term an agent or any other bailee intrusted with the care and management of the property of another. It is certain that they are not technically trustees. They can only be regarded as mandatories, persons who have gratuitously undertaken to perform certain duties, and who are, therefore, bound to apply ordinary care and diligence and no more." The directors are not technically trustees,[3] but they are agents who bear a relation of trust and confidence to their principal. They stand in a fiduciary relation to the corporation and are held to the utmost good faith in their dealings with it.[4] They must manage

see Skinner v. Walter, etc., Co., 140 N. Y. 217, executive committee, see Tracy v. Guthrie, etc., Soc., 47 Iowa 27.

[1] Spering's App., 71 Pa. St. 11, 10 Am. Rep. 684; Robinson v. Smith, 3 Paige (N. Y.), 222, 24 Am. Dec. 216. In re Cameron's, etc., R. Co., 18 Beav. 339; Overseers v. Gibbs, L. R. 5 H. L. 480.

[2] Spering's App., 71 Pa. St. 11.

[3] North Hudson, etc., Assn. v. Childs, 82 Wis. 460, 52 N. W. Rep. 600; Wayne, etc., Co. v. Hammons, 129 Ind. 368, 27 N. E. Rep. 487. In Briggs v. Spaulding, 141 U. S. 132, the court said: "The relation between the corporation and the directors is rather that of principal and agent, certainly so far as creditors are concerned, between whom and the corporation the relation is that of contract, and not of trust. But, undoubtedly, under circumstances they may be treated as occupying the position of trustees to *cestui que trust*." In Mulvane v. O'Brien, 58 Kan. 463, it was said that the directors and managing officers are *quasi* or *sub modo* trustees for the corporation with respect to corporate property, and for the stockholders with respect to their shares.

[4] Hoyle v. Plattsburgh, etc., R. Co., 54 N. Y. 314; Cumberland, etc., Co. v. Sherman, 30 Barb. 553; Wardell v. Union Pac. R. Co., 103 U. S. 651; Koehler v. Black River Falls, etc., Co., 2 Black (U. S.) 715. In Twin Lick, etc., Co. v. Marbury, 91 U. S. 587, Mr. Justice Miller said: "That a director of a corporation occupies one of the fiduciary relations where his dealings with the subject-matter of the trust or agency, and with the beneficiary or party whose interest is confided to his care, is viewed with jealousy by the courts, and may be set aside on very slight grounds, is a doctrine founded on the soundest morality, and which has received the clearest recognition in this court and in others."

its business with a view to promoting the common interests, and can not directly or indirectly derive personal profit or advantage from their position which is not shared by all the stockholders. By assuming the office they undertake to give their best judgment to the interests of the corporation in all matters in which they act for it, untrammeled by any conflicting personal interests. This obligation, that he will in no way use his position to advance his personal interest to the detriment of the corporation, is inherent in the office of director. All secret profits received by a director in any transaction in connection with corporate affairs must be accounted for to the corporation, although the transaction may also be of advantage to the corporation.[1] "The entire duty of the directors, growing out of their agency, is owed to the bank, which, under the charter, is the sole representative of the stockholders, and the legal defender of their properties.[2] A director who loans the money of the bank at a stipulated rate of interest, with a secret understanding that he shall have an interest in the profits on lands to be purchased with the money must account to the bank for such profits."[3] Where the directors of a corporation bought a steamboat in their individual capacity, and then, as directors of the corporation, purchased for the corporation a one-half interest in the boat at a greatly increased price, the corporation was held entitled to the profits arising from the transaction.[4]

The relations of a director and stockholder to the corporation are radically different. The latter may deal with the corporation to his personal benefit and profit,[5] while the former

[1] Bird, etc., Co. v. Humes, 157 Pa. St. 278. See also Parker v. Nickerson, 112 Mass. 195; Perry v. Cotton Seed Oil, etc., Co., 93 Ala. 364; Rutland, etc., Co. v. Bates, 68 Vt. 579.

[2] Allen v. Curtis, 26 Conn. 456.

[3] Koehler v. Iron Co., 2 Black (U. S.) 715.

[4] Parker v. Nickerson, 112 Mass. 195. In some cases it is held, on the theory that when a corporation becomes insolvent its property becomes a trust fund for the benefit of its creditors, that thereafter the directors are trustees for the benefit of the creditors. See Ingwersen v. Edgecombe (Neb.), 60 N. W. Rep. 1032.

[5] Rogers v. Nashville, etc., R. Co., 91 Fed. Rep. 299.

may not. It is sometimes said that the directors are trustees for the shareholders; but this means no more than that they are bound to act for the benefit of all the shareholders alike, and not for the benefit of themselves or any particular stockholder. "There is," said Chief Justice Shaw,[1] "no legal privity, relation or immediate connection between the holders of shares in a bank in their individual capacity on the one side and the directors of the bank on the other. The directors are not the bailees, factors, agents or trustees of such individual stockholders."

§ 503. **Contracts between a corporation and its officers.**— An officer of a corporation has no power when acting for the corporation to bind the coporation by a contract with himself, or to represent it in any transaction with third persons in which he has a personal interest.[2] As said by the supreme court of Wisconsin:[3] "The idea that the same persons constitute different identities of themselves by being called directors or officers of a corporation, so that as directors or officers they can convey or mortgage to or contract with themselves as private persons, is a violation of common

[1] Smith v. Hurd, 12 Met. (Mass.) 371; Lexington, etc., Co. v. Page & Richardson, 17 B. Mon. (Ky.) 412.

[2] McGourkey v. Toledo, etc., R. Co., 146 U. S. 536; Wardell v. Union Pac. R. Co., 103 U. S. 651; Rhodes v. Webb, 24 Minn. 292; Jones v. Morrison, 31 Minn. 140. Directors are not trustees for the corporation in the technical sense of the word; but they are prohibited from dealing with the *cestui que trust*; and if they disregard the duties and proprieties of the position by undertaking to represent their own interests and those of the corporation at the same time, they "will not be encouraged in thus walking in the path of temptation, nor be permitted to retain the fruits gathered while in pursuit of their own advancement, while they should have pursued none other than that of the corporation." Memphis, etc., R. Co. v. Woods, 88 Ala. 630, 16 Am. St. Rep. 81. Where the director is not at the same time representing his own interest and that of the corporation he may contract with it, buy or sell property, borrow its money and give his note therefor, or loan the money and take in consideration therefor its notes and enforce their payment in case of default. Ward v. Polk, 70 Ind. 309; Beach v. Miller, 23 Ill. App. 151; Garrett v. Burlington, etc., Co., 70 Iowa 697, 59 Am. Rep. 461; Ten Eyck v. P. O., etc., R. Co., 74 Mich. 226, 16 Am. St. Rep. 633.

[3] Haywood v. Lumber Co., 64 Wis. 639, 26 N. W. Rep. 184; People v. Board, 11 Mich. 222; Miner v. Ice Co., 93 Mich. 97.

sense." It is held that a director has no authority to represent his corporation in a transaction with another corporation in which he is a stockholder.[1] But the interest which will disqualify him from acting must be a real and substantial one, such as would be likely to induce the agent to sacrifice the interest of his principal.[2] Such cases are, of course, governed by the general rule that officers or directors may not gain advantage to themselves through their control of the corporation, as "they hold a place of trust, and by accepting the trust are obligated to execute it with fidelity, not for their own benefit, but for the benefit of the corporation."[3] The rule is not changed by the fact that other parties who stand in no trust relation to the corporation are interested in the transaction.[4] It applies when the transaction is with a firm of which the director is a member,[5] or another corporation in which he is a stockholder[6] or director.[7] But by the great weight of authority, contracts between directors and their corporations are voidable and not void.[8] "The duty which disqualifies directors from binding the corporation in a transaction in which they have an adverse interest is one owing to the corporation which they represent and to the stockholders thereof. A principal may consent to be bound by a contract made for it by an agent who at the same time represents an interest adverse to that of the principal. A *cestui que trust* may elect to affirm a contract which he could have repudiated on the ground that the trustee had an interest in the matter inconsistent with his trust relation. In like manner, dealings between a corporation represented by some person as director may be accepted as binding by the corporation or the stockholders

[1] Construction company, Gilman, etc., R. Co. v. Kelly, 77 Ill. 426.

[2] Bank v. Flour Co., 41 Ohio St. 552; Bristol v. Scranton, 63 Fed. Rep. 218.

[3] Koehler v. Black River Falls Co., 2 Black (U. S.) 715.

[4] Munson v. Railway Co., 103 N. Y. 58.

[5] Aberdeen R. Co. v. Blaikie, 1 Macq. H. L. 461.

[6] Parker v. Nickerson, 112 Mass. 195.

[7] United States, etc., Co. v. Atlantic, etc., R. Co., 34 Ohio St. 450.

[8] Little Rock, etc., R. Co. v. Page, 35 Ark. 304; Kelley v. Newburyport, etc., Co., 141 Mass. 496; Manufacturers' etc., Bank v. Big Muddy, etc., Co., 97 Mo. 38; United States, etc., Co. v. Atlantic, etc., Co., 34 Ohio St. 450, 32 Am. Rep. 380.

thereof. The general rule is that such dealings are not absolutely void, but are voidable at the election of the corporation or the stockholders thereof. They become binding if acquiesced in by the corporation. * * * The directors of a corporation, in the transaction of its business and the disposition of its property, do not sustain any such relation to the general creditors of the corporation as they occupy to the corporation and its stockholders. They are not the agents of such creditors, nor can they generally be regarded as trustees, acting in their behalf. The creditors are not entitled to disaffirm the transfer of the property of the corporation made by its director or other agent, merely because the corporation itself or its stockholders could have done so. The right of the creditors to impeach the transaction depends upon its fraudulent character.'"[1]

§ 504. **When an officer may deal with his corporation.**[2]— Notwithstanding the general language used in many decisions, there is no rule of law which absolutely prohibits an officer or director of a corporation from contracting with the corporation. The contract is merely voidable, and may therefore be accepted by the corporation. If it is represented by another agent in the transaction the reason for the general rule fails. The supreme court of the United States says:[3] "It can not be main-

[1] See, generally, notes to 17 Am. St. Rep. 300, *et seq*; 16 Am. St. Rep. 639.

[2] O'Connor, etc., Co. v. Coosa, etc., Co., 95 Ala. 614, 36 Am. St. Rep, 251. A director acting in a *quasi*-legislative capacity as a member of the board is incompetent to act in matters in which his interest is adverse to that of the corporation. The interested director may be counted as one of the persons necessary to constitute a quorum, and if the resolution could have been adopted with him voting against it, the mere fact that his presence was necessary to constitute a quorum will not deprive the resolution of its validity. Buell v. Buckingham & Co., 16 Iowa 284, 85 Am. Dec. 516. His vote can not properly be counted, however, if it is necessary to constitute a majority, if the question is one in which he is personally interested, and if, without his vote, the resolution could not have been carried by the requisite number of votes. In other words, it is not adopted at all; and he can not enforce any claim or right which is based solely upon it. Bennett v. St. Louis, etc., Co., 19 Mo. App. 349; Chamberlain v. Pacific, etc., Co., 54 Cal. 103; Copeland v. Johnson, etc., Co., 47 Hun 235; Smith v. Los Angeles, etc., Assn., 78 Cal. 289, 12 Am. St. Rep. 53.

[3] Twin Lick, etc., Co. v. Marbury, 91 U. S. 587.

tained that any rule forbids one director among several from lending money to the corporation when the money is needed, and the transaction is open and free from blame. No adjudged case has gone so far as this. Such a doctrine, while it would afford little protection to the corporation against actual fraud or oppression, would deprive it of the aid of those most interested in giving aid judiciously, and best qualified to judge of the necessity of that aid, and of the extent to which it may safely be given." The true rule is that a director or officer of a solvent corporation may deal with it, loan it money and take security therefor, if the transaction is fair and no advantage is taken of his position.[1] The transaction will be carefully scrutinized, but if it appears that it was in good faith and beneficial to the corporation, and the stockholders with full knowledge received the benefits, it will be upheld in a court of equity.[2] Hence, an officer or agent may purchase property and afterward sell it to the corporation if he was not guilty of a breach of duty in the purchase. The same principle will permit him to purchase a claim at a discount and afterward enforce it

[1] St. Joe, etc., Co. v. Bank, 10 Colo. App. 339, 50 Pac. Rep. 1055; Twin Lick, etc., Co. v. Marbury, 91 U. S. 587; Harts v. Brown, 77 Ill. 226; Mullanphy Bank v. Schott, 34 Ill. App. 500, affirmed in 26 N. E. Rep. 640; Beach v. Miller, 130 Ill. 162; Roseboom v. Whittaker, 132 Ill. 81; Louisville, etc., R. Co. v. Carson (Ill.), 38 N. E. Rep. 140. If the circumstances are such that a director may contract with a corporation, he may, of course, enforce his claim. Holt v. Bennett, 146 Mass. 437; Hallam v. Indianola, etc., Co., 56 Iowa 178. A director may become the purchaser at a mortgage foreclosure sale of the property of the corporation. Saltmarsh v. Spaulding, 147 Mass. 224. Also at an execution or judicial sale, although it is probable that the corporation might elect to compel him to hold the property for its benefit, or to disaffirm the sale and have the property resold. Hoyle v. Plattsburg, etc., R. Co., 54 N. Y. 314, 13 Am. Rep. 595; McAllen v. Woodcock, 60 Mo. 174; Raleigh v. Fitzpatrick, 43 N. J. Eq. 501.

[2] Keystone, etc., Co. v. Bate, 187 Pa. St. 460; Barr v. Pittsburgh, etc., Co., 57 Fed. Rep. 86; Gorder v. Plattsmouth, etc., Co. (Neb. 1893), 41 Am. & Eng. Corp. Cas. 87; Keeney v. Converse (Mich. 1894), 58 N. W. Rep. 325; Twin Lick, etc., Co. v. Marbury, 91 U. S. 587; Leavenworth v. Chicago, etc., Co., 134 U. S. 688; Battelle v. Northwestern, etc., Co., 37 Minn. 89; Garrett v. Plow Co., 70 Iowa 697; Welch v. Bank, 122 N. Y. 177; Holt v. Bennett, 146 Mass. 437; Saltmarsh v. Spaulding, 147 Mass. 224.

in full against the corporation.[1] But a purchase of land by a director from the corporation at a greatly inadequate price raises a presumption of fraud and throws upon the officer the burden of showing the good faith of the transaction.[2]

If it is apparent that a contract or other business transaction between a director and the corporation was not attended by collusion between him and his fellow-direct-

[1] Morawetz Priv. Corp. I, § 521, approved in St. Louis, etc., R. Co. v. Chenault, 36 Kan. 51.

[2] Woodruff v. Howes, 88 Cal. 184. In Miner v. Belle Isle, etc., Co., 93 Mich. 97, McGrath, J., said: "The authorities upon the question of the validity of contracts made by directors with corporations are by no means harmonious. It is laid down in many of the text-books that such contracts are voidable at the instance of the corporation. 1 Beach Corp., §§ 241, 242; Morawetz Corp., §§ 243–245; Taylor Corp., §§ 629, 630; 2 Field Briefs, 193. Again it has been held that a director may deal with the company in like manner as with an individual, if he deals honorably, and without endeavoring to influence or control it. 16 Am. Law Rev. 917; Harts v. Brown, 77 Ill. 226; United States, etc., Co. v. Atlantic, etc., R. Co., 34 Ohio St. 450; Mayor v. Inman, etc., Co., 57 Ga. 370. Our own courts, in People v. Overyssel, 11 Mich. 222, and in Railway Co. v. Dewey, 14 Mich. 477, have held that such contracts were not only voidable but absolutely void. * * * All the authorities agree that it is essential that the majority of the quorum of a board of directors shall be disinterested in respect to the matter voted upon." 1 Beach Corp., 276; Smith v. Association, 78 Cal. 289. Where a loan board of three are authorized to make a grant to a railroad, and two of them, one being director of the railroad, make the grant, the court will set it aside. San Diego v. Railroad Co., 44 Cal. 106; Bill v. Telegraph Co., 16 Fed. Rep. 14. A salary voted to the president by a quorum of directors, two being absent, and the president being one of the three, is not enforcible. Copeland v. Manufacturing Co., 47 Hun 235. Where the chief stockholder, who is president, induces the directors, his dummies, to vote a large salary to him, the corporation may defeat the officers' action at law to recover it. Davis v. Railroad Co., 22 Fed. Rep. 883. Where the majority of stock of a corporation was held by one family, who voted away the corporate profits for salaries, the minority may call upon a court of equity to remedy the fraud. Sellers v. Iron Co., 13 Fed. Rep. 20. A stockholder may compel the contractors to disgorge when they obtain a contract through their associates or hirelings being made directors. Currier v. Railroad Co., 35 Hun (N.Y.) 355. When two contractors cause a railroad corporation to be formed, in which one contractor becomes a director, and the other directors are clerks of the second contractor, and the construction control is made with these two by means of dummy intermediaries, at an improvident price, one of the contractors can not compel the other to divide the profits. Jackson v. McLean, 36 Fed. Rep. 213. See Hirsche v. Sims (H. L. 1894), L. R. (1894), A. C. 654.

ors; that they represented the corporation according to their best judgment; that the contract was open, fair and without concealment on the part of the contracting director, and without taking advantage of any information which he may have had to the exclusion of his fellow-directors, it is enforcible both at law and in equity, whether the corporation acquiesces in or resists such enforcement.[1] The Iowa Supreme Court declined to consent to the proposition "that a director of an insolvent corporation can not take from it security by mortgage or other conveyance, securing a lien upon its property, even though acting in good faith and without fraud in the transaction. A creditor may accept payment or security from an insolvent debtor free from the claim of other creditors. A corporation may make payment of its debts, or give its property in security thereof, just as any person may do. If, therefore, the director holds the indebtedness of an insolvent corporation he may take payment or security, if an honest transaction. No reason can be given why a director who holds a valid debt against his corporation can not, though it be insolvent, in a fair and honest way take its property in security. If the property, money or other consideration for the debt was fairly used for the benefit of the corporation, was added to its assets and used in its business, it would be unreasonable to hold that the director is deprived of the remedy held by other creditors."[2] Therefore, a contract between a corporation and one of its directors, which is open, fair and free from fraud, and sanctioned by a majority of the board of directors, not including himself, is binding upon the corporation.[3] Such transac-

[1] Beach v. Miller, 130 Ill. 162, 17 Am. St. Rep. 291; Watts' App., 78 Pa. St. 370; Garrett v. Burlington, etc., Co., 70 Iowa 697, 59 Am. Rep. 461.

[2] Garrett v. Burlington, etc., Co., 70 Iowa 697, 59 Am. Rep. 461. See also Stetson v. Northern, etc., Co., 104 Iowa 393. A director's note for his own salary will not render the proceedings void when the result would have been the same if he had not voted. Clark v. American, etc., Co., 86 Iowa 436, 17 L. R. A. 557.

[3] Twin-Lick, etc., Co. v. Marbury, 91 U. S. 587; Barr v. Plate Glass Co., 57 Fed. Rep. 86, 17 U. S. App. 124; Roseboom v. Whittaker, 132 Ill. 81, 23 N. E. Rep. 339; Louisville, etc., R. Co. v. Carson, 151 Ill. 444; Hallam v. Hotel Co., 56 Iowa 178, 9 N. W. Rep.

tions will, however, be carefully scrutinized by the courts,[1] and the burden is on the officer to show that it is free from fraud and fair to the corporation.[2] Where a disinterested majority of the board of directors assent, the binding force of the contract is made to turn upon the fairness or unfairness of the contract to the corporation. But there are some jurisdictions in which the corporation is permitted to repudiate the contract upon showing the mere fact of the relation.[3]

§ 505. **Right of corporation to repudiate such contract.**—A corporation may repudiate or ratify any transaction entered into by its agents or officers without authority, if it is of a character which it might have originally authorized.[4] The right to repudiate is, however, subject to the provision that the corporation must return the property or money which it received from the agent under the contract.[5] As already stated, a corporation can not repudiate a contract between it and one of its officers or directors, which is fair and honest, and in the

111; Garrett v. Plow Co., 70 Iowa 697; Buell v. Buckingham & Co., 16 Iowa 284; Parker v. Nickerson, 137 Mass. 487; Holt v. Bennett, 146 Mass. 437; Saltmarsh v. Spaulding, 147 Mass. 224; Ten Eyck v. Railroad Co., 74 Mich. 226. See Miner v. Belle Isle, etc., Co., 93 Mich. 97.

[1] Thomas v. Railroad Co., 109 U. S. 522.

[2] Jones v. Morrison, 31 Minn. 140; Wilkinson v. Bauerle, 41 N. J. Eq. 635.

[3] See Munson v. Railroad Co., 103 N. Y. 58; Barr v. New York, etc., R. Co., 125 N. Y. 263; Hoyle v. Railroad Co., 54 N. Y. 314; Pearson v. Railroad Corp., 62 N. H. 537.

[4] Hoffman, etc., Co. v. Cumberland, etc., Co., 16 Md. 456, 77 Am. Dec. 311; Hotel Co. v. Wade, 97 U. S. 13; Stewart v. Lehigh Valley R. Co., 38 N. J. L. 505; Meeker v. Iron Co., 17 Fed. Rep. 48; Thomas v. Railway Co., 109 U. S. 522. Dealings between corporations represented by the same officers and directors may be accepted as binding by each corporation and the stockholders thereof, as such dealings are not absolutely void but merely voidable at the election of the directors or the stockholders; and they become binding if acquiesced in by the corporation and the stockholders. O'Conner, etc., Co. v. Coosa, etc., Co., 95 Ala. 614, 36 Am. St. Rep. 251; Buell v. Buckingham & Co., 16 Iowa 284; Ashhurst's App., 60 Pa. St. 290. See also note to Beach v. Miller, 17 Am. St. Rep. 298. It stands on practically the same ground as a transaction between a trustee and a *cestui que trust* in that it may be avoided by the *cestui que trust*, if he repudiates it within a reasonable time after it comes to his knowledge. Buell v. Buckingham & Co., 16 Iowa 284; Ashhurst's App., 60 Pa. St. 290.

[5] Gardner v. Butler, 37 N. J. Eq. 702.

making of which the corporation is represented by other disinterested agents. All contracts made by a corporate officer with a corporation are, at the most, merely voidable at the election of the corporation, and therefore binding upon the corporation until repudiated.[1] This must be done within a reasonable time after knowledge of the facts.[2] Such a contract can not be avoided when all those who are interested in the corporation consented that it might be made, and the property received under the contract is retained by the corporation.[3]

§ 506. **Contracts between corporations having common officers or directors.**—It has been held in a few cases that a contract between corporations having common officers or directors is presumably fraudulent, and may be avoided irrespective of its merits, although there was a majority in favor of making the contract without counting the common directors. In some of these decisions it is said that the contract is void; in others that there is a conclusive presumption of fraud, while others merely say that there is a presumption of fraud, and that when this is overcome by evidence which discloses a fair and honest contract, it will be sustained.[4] Under such circumstances, that is, where a director is incapable of making a contract, it may, nevertheless, become binding by the acquiescence of the shareholders.[5]

§ 507. **The prevailing rule.**—The weight of authority is against the strict rule which renders all contracts between corporations having common officers or directors void.

[1] Twin Lick, etc., Co. v. Marbury, 91 U. S. 587; Barr v. New York, etc, R. Co., 125 N. Y. 263.

[2] See Twin Lick, etc., Co. v. Marbury, 91 U. S. 587.

[3] Battelle v. Pavement Co., 37 Minn. 89. See Barr v. Glass Co., 57 Fed. Rep. 89.

[4] Metropolitan, etc., R. v. Manhattan, etc., Co., 14 Abbott N. Cas. 103, 272–294, 11 Daly 373; O'Conner, etc., Co. v. Coosa, etc.. Co., 95 Ala. 614; Fitzgerald v. Fitzgerald, etc., Co., 44 Neb. 463; Currier v. New York, etc., R. Co., 35 Hun (N. Y.) 355; Sweeny v. Wheeling, etc., Co., 30 W. Va. 443. Under the Engish statute, 7 and Vict., ch. 10, section 29, which prohibits a director from voting on a contract in which he is interested, it is held that a contract, in the making of which this provision is violated, is void. See Ernest v. Nicholls, 6 H. L. Cas. 401.

[5] O'Conner, etc., Co. v. Coosa, etc., Co., 95 Ala. 614.

Where two corporations, through their boards of directors, make a contract with each other, the common directors are not within the rigid rule of the cases which hold that one who acts in a fiduciary capacity can not deal with himself in his individual capacity, and that any contract thus made will be declared void, without reference to its fairness or the benefits derived from it by the *cestui que trust*. Two corporations have the right, within the scope of their chartered powers, to deal with each other; and this right is not destroyed or paralyzed by the fact that some of the directors are common to both. Of course, if such directors should wrongfully and willfully use their powers to the prejudice of one of the corporations, their action, if not acquiesced in and if not contested at the proper time, can be avoided as in any other case of actual fraud. But such common directors owe the same fidelity to both corporations, and there is no presumption that they will deal unfairly with either. While their acts may be voidable they certainly are not void.[1] It is proper that a contract of this character should be subjected to close scrutiny,[2] and if it appears that there was actual fraud or any advantage was of either corporation, it should be set aside.[3] The same rule

[1] San Diego, etc., Co. v. Pacific etc., Co. (Cal.), 33 L. R. A. 788; Pauly v. Pauly, 107 Cal. 8, 48 Am. St. Rep. 98; Adams, etc., Co. v. Senter, 26 Mich. 73; Leavenworth Co. Com. v. Chicago, etc., R. Co., 134 U. S. 688; Coe v. East, etc., R. Co., 52 Fed. Rep. 531; Bill v. W. U. Tel. Co., 16 Fed. Rep. 14; Flagg v. Manhattan, etc., R. Co., 10 Fed. Rep. 413; Jesup v. Illinois Central R. Co., 43 Fed. Rep. 483; Booth v. Robinson, 55 Md. 419; United States, etc., Co. v. Atlantic, etc., Co., 34 Ohio St. 450, 32 Am. Rep. 380; Roberts v. Washington Nat'l Bank, 11 Wash. 550. When contracts are entered into between two corporations, a majority of the boards of directors of the two corporations being the same persons, and the interests which they represent being adverse, the contracts may be set aside at the instance of any person having an interest which may have been sacrificed. Such contracts may be sustained by proving that the directors, although they represented conflicting interests, acted in good faith. Pearson v. Concord, etc., R. Co., 62 N. H. 537, 13 Am. St. Rep. 590; Goodin v. Cincinnati, etc., Co., 18 Ohio St. 169, 98 Am. Dec. 95; Memphis, etc., R. Co. v. Woods, 88 Ala. 630, 16 Am. St. Rep. 81.

[2] Roy, etc., Co. v. Scott, etc., Co., 11 Wash. 399; Langan v. Francklyn, 29 Abbott N. Cas. 102; Davidson v. Mexican, etc., R. Co., 58 Fed. Rep. 653.

[3] Union Pac. R. Co. v. Mobilier, 135 Mass. 367.

applies to contracts between corporations having the same executive officers as well as directors. Thus, a valid contract may be made between two corportions which have the same president.[1] Contracts which might have been avoided by the corporation may become binding by ratification.[2] The unanimous consent of all the stockholders is not necessary to the ratification of a voidable or unauthorized contract, as acts which might have been authorized by the majority may be ratified by the majority. "The corporation may, however, ratify an unauthorized transaction of its agents; and this may be done by the unanimous acquiescence of the shareholders, or by vote of the majority, if the transaction was of such a character that the majority might have authorized it at the outset."[3]

§ 508. **Liability of a corporation for torts of its agents.**[4]— The general question of the liability of corporations for torts has already been considered.[5] Their liability for the torts of their agents is governed by the general law of agency. As a general proposition a corporation is liable for the torts of its officers and agents when committed in the course of their actual or apparent employment. If the act is expressly authorized, or is ratified by proper authority, there is, of course, no question as to the liability of the corporation for the resulting damages. If the corporation confers upon an agent the apparent authority to do an act, it can not escape responsibility for the wrongful manner in which the act is done by the person whom it

[1] McComb v. Barcelona, etc., Assn., 134 N. Y. 598; Mayor v. Inman, etc., Co., 57 Ga. 370.

[2] San Diego, etc., R. Co. v. Pacific, etc., Co. 112 Cal. 53, 33 L. R. A. 788. For illustrations of what constitutes ratification, see Roberts v. National Bank, 11 Wash. 550; United States, etc., Co. v. Atlantic, etc., Co., 34 Ohio St. 450, 32 Am. Rep. 380; Kitchen, etc., Co. v. St. Louis, etc., Co., 69 Mo. 224; Evansville, etc., Co. v. Bank (Ind.), 42 N. E. Rep. 1097. Before such a contract can be avoided it is necessary that what has been received under it be returned. Thomas v. Brownville, etc., R. Co., 109 U. S. 522.

[3] Morawetz Priv. Corp., § 525, quoted in San Diego, etc., R. Co. v. Pacific, etc., Co., 112 Cal. 53.

[4] See Wilgus' Cases, Liability of Corporations for Torts.

[5] See ch. 10, *supra*.

thus holds out to the world as authorized to represent it in such matters. But if the wrongful act is not done under actual or apparent authority, the responsibility for it can not be transferred from the agent to the corporation. A corporation is liable for the tortious acts of its agent when a natural person would be liable for the act under the same circumstances.[1] Hence the statement of the rule as to natural persons by Story[2] is equally applicable to corporations: "A principal is to be held liable to third persons in a civil suit for the frauds, deceits, concealments, misrepresentations, negligences and other malfeasances and misfeasances and omissions of duty of his agent in the course of his employment, although the principal did not authorize or justify or participate in, or indeed, know of such misconduct, or even if he forbade the acts or disapproved of them. In all such cases the rule applies *respondeat superior*, and is founded upon public policy and convenience, for in no other way could there be any safety to third persons in their dealings directly with the principal or indirectly with him through the instrumentality of agents. In every such case the principal holds out his agent as competent and fit to be trusted, and thereby in effect warrants his fidelity and good conduct in all matters within the scope of his agency."

If the act was done in the course of the agent's employment, the corporation can not escape liability on the ground that it was unauthorized, or that it was expressly forbidden, nor does the fact that the agent acted willfully or maliciously affect the question.[3] Thus, a railroad company is liable in damages for an assault by its conductor upon a passenger.[4] But the agent represents the corporation only when acting for it within the actual or apparent scope of his authority, and it has been therefore held that a street railway company is not liable for malicious prosecution and false arrest by its president and

[1] Denver, etc., R. Co. v. Harris, 122 U. S. 697; Fifth Avenue, etc., Bank v. Forty-second St., etc., Co., 137 N. Y. 231.

[2] Agency, § 452.

[3] Wheeler, etc., Co. v. Boyce, 36 Kan. 350.

[4] North Chicago, etc., R. Co. v. Gastka, 128 Ill. 613; Dwinelle, etc., R. Co. v. Railway Co., 120 N. Y. 117; Cracker v. Railway Co., 36 Wis. 657.

superintendent on a charge of passing counterfeit money by dropping a lead coin in the fare box.[1] Nor is a corporation liable for the fraud of its president, who in negotiating a loan to himself falsely represents that certain certificates of stock in the corporation, which he offers as collateral for the loan, are genuine.[2] A corporation is not liable for the act of its manager, who received certain certificates of stock with directions to cancel them, but who fraudulently reissued them for his own benefit.[3] In these cases the act was not within the actual or apparent authority conferred by the corporation upon the agent; and in order to hold the corporation it would be necessary to show that the specific act was either expressly authorized or ratified.[4]

§ 509. **Ratification.**—A corporation may become liable for the unauthorized torts of its agent by ratification, either expressly, or through the acceptance of the benefits arising therefrom with knowledge of the facts and circumstances. Thus, where the agents of a corporation organized for educational purposes, wrongfully engaged in the business of conveying passengers from the railway station to the grounds of its school buildings, it was held liable for personal injuries occasioned by the negligence of such agents, where it appeared that the managing officers knew that the business was being carried on, and received and retained the income resulting therefrom.[5]

[1] In Central, etc., Co. v. Brewer, 78 Md. 394, 27 L. R. A. 63, it was held that the superintendent of a street railway company has no implied authority to cause the arrest of a passenger for putting counterfeit coin in a fare box; and the fact that the president, superintendent and driver testified before the court afforded no legally sufficient evidence of ratification or adoption. If they were without authority in causing the arrest, the subsequent testimony given for the state by them, or the manner in which they demeaned themselves in delivering their testimony, did not support the theory of adoption or ratification.

[2] Manhattan, etc., Co. v. Forty-second St., etc., Co., 139 N. Y. 146. See Moores v. Bank, 111 U. S. 156.

[3] Knox v. Eden Musee, etc., Co., 148 N. Y. 441.

[4] See Central R. Co. v. Brewer, *supra*.

[5] Nims v. Mt. Hermon, etc., School, 160 Mass. 177, 22 L. R. A. 364, Wilgus' Cases; Eastern, etc., R. Co. v. Broom, 6 Exch. 314, Wilgus' Cases.

§ 510. **Liability for torts in ultra vires transactions.**—When it is sought to hold a corporation liable for the torts of its agents, the only question properly for consideration is the authority of the agent. In some cases, however, the courts have said that the employment of the agent must have been in a transaction in which it was within the power of the corporation to engage. If the act was *ultra vires*, it was said that the corporation could not authorize it to be done by its agent, and that therefore there was no liability of the corporation for the tortious acts of the agent committed in the course of the *ultra vires* transaction.[1] Thus, in Maryland, where it was sought to hold a national bank liable for false representations made by its teller, in the sale of certain bonds, the court said: "We are clearly of the opinion that the business of selling bonds on commission is not within the scope of the powers of the corporation, and the bank could not, under any circumstances, carry it on; and being thus beyond the corporate powers, the defense of *ultra vires* is open to the appellee. And it follows from this that the bank is not responsible for any false representations made by its teller to the appellant, by which she was induced to purchase the bonds in question."[2] So, in Georgia, an action against a railroad corporation and an individual as partners failed because it was held that the corporation had no power to become a member of a partnership.[3] But the rule now established is that, if a corporation engages in an *ultra vires* transaction, it is liable for the torts of its agents, committed under apparent authority in the course of the transaction. This rule is strongly stated in the well known Bissell case,[4] where the distinction between the power and capacity, as distinguished from the *right* to do an act, was noted, and certain railroad corporations operating their roads jointly under an *ultra vires* act were held liable for personal injuries

[1] Bathe v. Society, 73 Iowa 11.

[2] Weckler v. Bank, 42 Md. 581.

[3] Ginn v. Railway Co., 74 Ga. 509.

[4] 22 N. Y. 258. See also Buffett v. Railway Co., 40 N. Y. 168; Central, R. etc., Co. v. Smith, 76 Ala. 572; New York, etc., R. Co. v. Haring, 47 N. J. L. 137; Hutchinson v. Railway Co., 6 Heisk. (Tenn.) 634; Nims v. Mt. Hermon School, 160 Mass. 177, 39 Am. St. R. 467, 22 L. R. A. 364, Wilgus' Cases.

caused to a passenger through the negligence of their agents. Where a street railway corporation attempted to avoid liability for a personal injury, on the ground that it was engaged in an *ultra vires* transaction, not having been granted the necessary franchise, the court said:[1] "But the doctrine of *ultra vires* does not apply to torts of this nature. It would indeed be an anomalous result in legal science if a corporation should be permitted to set up that, inasmuch as a branch of the business prosecuted by it was wrongful, therefore all the special wrongs done to individuals in the course of it were remediless. But in such situations corporations, like individuals, can not take advantage of their own wrong by way of defense. If corporations are not to be held responsible for injuries done to persons in the transaction of a series of wrongful acts, such an immunity would have wide scope. All wrongs done by such bodies are in a sense *ultra vires*, and if the want of a franchise to do a tortious act be a defense, then corporations have a dispensation from liability for these acts peculiar to themselves."

§ 511. **Liability of officers for acts in excess of authority.**— Directors and other officers who exceed their authority may be liable not only to the corporation for any damages occasioned thereby to it, but also personally to the parties with whom they have dealt.[2] "There can be no doubt that if the directors or officers of the company do acts clearly beyond their power whereby loss ensues to the company, or dispose of its property, or pay away its money without authority they will be required to make good the loss out of their private estate."[3] This is the rule whether the disposition made of the money or property of the corporation is one either not within the lawful power of the corporation, or if within the power of the corpo-

[1] New York, etc., R. Co. v. Haring, 47 N. J. L. 137.

[2] Solomon v. Penoyar, 89 Mich. 11; Citizens', etc., Assn. v. Coriell, 34 N. J. Eq. 383; Nelligan v. Campbell, 20 N. Y. Supp. 234. But see Farmers' and Mechanics' Bank v. Colby, 64 Cal. 352.

[3] Thompson Liability of Officers, § 375; Discount Co. v. Brown, L. R. 8 Eq. 381; Flitcroft's case, L. R. 21 Ch. Div. 519; Insurance Co. v. Jenkins 3 Wend. 130.

ration, is not within the power or authority of the particular officer or officers.[1]

This liability for unauthorized acts, although prohibited by statute or by-law, rests in fact upon the common-law rule which renders every agent liable, who exceeds his authority or neglects his duty.[2] But the officer is not liable to the corporation for *ultra vires* acts which were authorized by the stockholders, either expressly or by acquiescence.[3] The fact that the board of directors in violation of their own duty attempted to authorize an officer to do an act in violation of his duty, is no defense to an action on the officer's official bond.[4]

§ 512. **Liability for abuse of trust.**—The directors of a private corporation who willfully abuse their trust or misapply the funds of the company by which a loss is sustained, are personally liable to make good the loss, and they are equally liable if they suffer the corporate funds or property to be wasted by gross neglect and inattention to the duties of their position.[5] So, if there is neglectful abandonment of his official duty by a director, or if he leaves the entire control of the company's business to other agents and fails to exercise proper supervision, he is liable for losses which due attention and diligence on his part might have prevented. If there is culpable negligence of this character on the part of a director, an action at law may be maintained against him by his principal, as in other cases of agency, without joining his associates.[6] An officer who has misappropriated the funds of a corporation

[1] North Hudson, etc., Assn. v. Childs, 82 Wis. 460, 52 N. W. Rep. 600.

[2] Briggs v. Spaulding, 141 U. S. 132; North Hudson, etc., Assn. v. Childs (Wis.), 52 N. W. Rep. 600; Throop Liability of Officers, § 357. As to what acts are sufficient to charge the officers, see Perry v. Tuscaloosa, etc., Co. (Ala.), 9 So. Rep. 217; Wayne, etc., Co. v. Hammons (Ind.), 27 N. E. Rep. 487; Ellis v. Ward, 137 Ill. 530, 25 N. E. Rep. 530.

[3] Holmes v. Willard, 125 N. Y. 75.

[4] Minor v. Bank, 1 Pet. (U. S.) 46.

[5] Doe v. N. W. & Co., 78 Fed. Rep. 62; Robinson v. Smith, 3 Paige 221, 24 Am. Dec. 212; Brinckerhoff v. Bostwick, 88 N. Y. 52; Delano v. Case, 121 Ill. 247; Perry v. Oil Mill Co., 93 Ala. 364; Wilkinson v. Bauerle, 41 N. J. Eq. 635; Marshall v. Bank, 85 Va. 676, 17 Am. St. Rep. 84.

[6] Horn, etc., Co. v. Ryan, 42 Minn. 196; Hun v. Cary, 82 N. Y. 65, 37 Am. Rep. 546; Empire, etc., Bank v. Beard, 30 N. Y. Sup. 756.

can not cure the breach of duty and entitle himself to the further custody of the assets by simply restoring the money.[1]

§ 513. **Degree of care required of directors.**[2]—Officers and directors of a corporation, when they act in good faith within their authority and the limits of the power conferred upon them by the charter, are not responsible to the corporation for losses resulting from mere mistakes of judgment. Their liability, if any, must result from a failure to exercise the ordinary care and diligence which is required from them under the circumstances. This degree of care is that which a prudent man exercises in his own affairs.[3] In a recent case[4] it was said: "In respect to directors, or those acting *ex officio* as such, the rule of liability has been the subject of much discussion. In the recent case of Briggs v. Spaulding,[5] in which, although there was a strong dissent, the rule may be regarded as settled, in the federal courts at least, and in the courts of several of the states as there laid down, and to the effect that directors, although often called trustees, are not such in any technical sense, but that they are mandataries, the relation between them and the corporation being rather that of principal and agent; but, under circumstances, they may be treated as occupying, in consequence of the powers conferred on them, the position of trustees to *cestuis que trustent;* that the degree of care required of them depends upon the subject to which it is to be applied, and each case is to be determined upon its own circumstances; that, as they render their services gratuitously, they are not to be held to the degree of responsibility of

[1] Fougeray v. Cord (N. J. Eq.), 24 Atl. Rep. 499.

[2] See Wilgus' Cases.

[3] Wallace v. Lincoln Sav. Bank, 89 Tenn. 630, 24 Am. St. Rep. 625; Sperring's App., 71 Pa. St. 11; 10 Am. Rep. 684; Hun v. Cary, 82 N. Y. 65, 37 Am. Rep. 546; Watts' App., 78 Pa. St. 370; Horn v. Silver, etc., Co., 42 Minn. 196; Williams v. McDonald, 37 N. J. Eq. 409; Mowbray v. Antrim, 123 Ind. 24, 23 N. E. Rep. 858. As to suspicious circumstances which should cause a director to make inquiry, see Gibbons v. Anderson, 80 Fed. Rep. 345; Robinson v. Hall, 63 Fed. Rep. 222, 25 U. S. App. 48, 12 C. C. A. 674. Note to 48 Am. St. Rep. 921.

[4] North Hudson, etc., Assn. v. Childs (Wis.), 52 N. W. Rep. 600.

[5] 141 U. S. 132. See, also, Warner v. Penoyer, 82 Fed. Rep. 181.

bailees for hire,[1] or expected to devote their whole time and attention to their duties; that they are not, in the absence of any element of positive misfeasance, and solely on the grounds of passive negligence, to be held liable, unless their negligence is gross, or they are fairly subject to the imputation of a want of good faith. * * * The degree of care they are bound to exercise is that which ordinary prudent and diligent men would exercise under similar circumstances in respect to a like gratuitous employment, regard being had to the usages of business and the circumstances of each particular case; that they are not liable, in the absence of fraud or intentional breach of trust, for negligence, mistakes of judgment and bad management in making investments on doubtful or insufficient security. Where they have not profited personally by their bad management, or appropriated any of the property of the corporation to their own use, courts of equity treat them with indulgence. Were a more rigid rule to be applied, it would be difficult to get men of character and pecuniary responsibility to fill such positions."[2]

§ 514. **Liability of officer is for individual acts or omissions.** —It is for their own acts and negligence only that officers and directors of a corporation are liable to the corporation. Hence, the corporation can not hold a director merely because he is a director personally liable for damages occasioned by the wrongful acts or negligence of other directors. "Upon a close examination of all the reported cases," said Mr. Justice Sharswood,[3] "although there are many *dicta* not easily reconcilable, yet, I have found no judgment or decree which has held directors to account, except when they have themselves been guilty of some fraud on the corporation or have known or connived at some fraud in others, or where such fraud might have been prevented had they given ordinary attention

[1] Hun v. Cary, 82 N. Y. 65; Horn, etc., Co. v. Ryan, 42 Minn. 196.

[2] Spering's App., 71 Pa. St. 11; Swentzel v. Bank (Pa.), 23 Atl. Rep. 405; In re Forest, etc., Co., L. R. 10 Ch. Div. 450; Ackerman v. Halsey, 37 N. J. Eq. 356; In re Denham & Co., 25 L. R. Ch. Div. 752; Watts' App., 78 Pa. St. 370; Hun v. Cary, 82 N. Y. 65.

[3] Spering's App., 71 Pa. St. 11.

to their duty. I do not mean to say by any means that their responsibility is limited to these cases, and that there might not exist such a case of negligence or of acts clearly *ultra vires* as would make perfectly honest directors liable. But it is evident that gentlemen selected by the stockholders from their own body ought not to be judged by the same strict standard as the agent or trustee of a private estate. Were such a rule applied, no gentleman of character and responsibility would be willing to accept such places.'"[1] The corporation has a remedy against the directors and officers for negligence, fraud, breach of trust, or for acts done in excess of their authority, but the case against each is distinct, depending upon the evidence against him, unless two or more have joined or participated in the wrongful act, in which case all participants may be joined as defendants.[2] The liability for acts of sub-agents is based upon the want of care in selecting or supervising such agents. Thus, the directors are not insurers of the fidelity of the agents whom they have appointed, who are not their agents, but the agents of the corporation, and they can not be held responsible for losses resulting from the wrongful acts or omissions of other directors or agents, unless the loss is a consequence of their own neglect of duty, either in failing to supervise the business with attention or in neglecting to use proper care in the appointment of agents.[3] It is no ground of liability or even of censure, that directors knowing of the bank's embarrassment, conceal the fact from creditors; for such is their duty, unless the embarrassment is such as to imperatively demand suspension.[4]

§ 515. **Supervision of sub-agents.**—With reference to the claim that the directors of a corporation should have exercised

[1] Association v. Coriell, 34 N. J. Eq. 383; Land, etc., Co. v. Lord Fermoy, L. R. 5 Ch 763.

[2] North Hudson, etc., Assn. v. Childs, 86 Wis. 292, 52 N.W. Rep. 600; Briggs v. Spaulding, 141 U. S. 132; Warner v. Penoyer, 82 Fed. Rep. 181.

[3] Briggs v. Spaulding, 141 U. S. 132. See also Wheeler v. Aiken Bank, 75 Fed. Rep. 781; Savings Bank v. Caperton, 87 Ky. 306; Stapleton v. Odell, 47 N. Y. Supp. 13; New York, etc., Co.v. Higgins, 29 N.Y. Supp. 416; Higgins v. Hayden (Neb.), 73 N. W. Rep. 280; Isham v. Post (N. Y.), 35 N. E. Rep. 1084.

[4] Robinson v. Hall, 59 Fed. Rep. 648.

greater care in checking up the books of a bank, and examining into the conduct of a managing officer, the supreme court of the United States said:[1] "Certainly it can not be laid down as a rule that there is an invariable presumption of rascality as to one's agents in business transactions, and that the degree of watchfulness must be proportioned to that presumption. 'I know of no law,' said Vice-Chancellor McCoun,[2] 'which requires the president or directors of any moneyed institution to adopt a system of espionage in relation to their secretary or cashier or any subordinate agent, or to set a watch upon all their actions. While engaged in the performance of the general duties of their station they must be supposed to act honestly, until the contrary appears; and the law does not require their employer to entertain jealousies and suspicions without some apparent reason. Should any suspicious circumstance transpire to awaken a just suspicion of their want of integrity, and it be suffered to pass unheeded, a different rule would prevail, if a loss ensued. But without some fault on the part of the directors amounting either to negligence or fraud, they can not be liable.'" It was therefore held that the failure of directors to cause a thorough examination of the books of the bank to be made within ninety days after their election was not negligence, when the bank was generally regarded as in good condition and the managing officer was a man of good reputation in the community.

§ 516. **Knowledge of contents of corporate records.**—A director or stockholder is not chargeable with actual knowledge of the business transactions of the corporation merely because he is such director or stockholder.[3] The directors of a corpo-

[1] Briggs v. Spaulding, 141 U. S. 132. In San Pedro, etc., Co. v. Reynolds, 121 Cal. 74, the manager of a corporation whose duties were to superintend, oversee, and direct the business of the corporation, was held liable for thefts by a bookkeeper, on the ground that they would have been avoided had he given proper attention to the business. See Cameron v. Kenyon-Connell, etc., Co. (Mont.), 44 L. R. A. 508.

[2] Scott v. DePeyster, 1 Ed. Ch. 513.

[3] Rudd v. Robinson, 126 N. Y. 113, 22 Am. St. Rep. 816. See Houston v. Thornton, 122 N. C. 365, 65 Am. St.

ration can not as a matter of law be charged with knowledge of what is disclosed by the books and records of the corporation. Thus, in an action in which it was sought to hold the directors liable for negligence the supreme court said that knowledge of what the books and papers would have shown can not be imputed to the directors.[1] Chief Justice Fuller quoted with approval the following language of Judge Earl:[2] "He was simply a director and as such attended some of the meetings of the board of directors. As he was a director, must we impute to him for the purpose of charging him with fraud a knowledge of all the affairs of the company? If the law requires this then the position of a director in any large corporation like a railroad or banking or insurance company, is one of constant peril. The affairs of such a company are generally of necessity largely intrusted to managing officers. The directors generally can not know and have not the ability or knowledge requisite to learn by their own efforts the true condition of the affairs of the company. They select agents in whom they have confidence and largely trust to them. They publish their statements and reports relying upon the facts and figures furnished by their agents; and if the directors, when actually cognizant of no fraud, are to be held liable in an action of fraud for an error or misstatement in such statements and reports, then we have a rule by which every director is made liable for any fraud that may be committed upon the company in the abstraction of its assets and diminution of its capital by any of its agents, and he becomes substantially an insurer of their fidelity. It has not been generally understood that such a responsibility rested upon the directors of a corporation and I know of no principle of law or rule of public policy which requires that it should."

On the same question Sir George Jessel said:[3] "It is contended that Hallmark, being a director must be taken to have

Rep. 699, annotated, 21 Am. St. Rep. 662. As to when knowledge of proceedings are to be imputed to officers and shareholders, see note to 22 Am. St. Rep. 821.

[1] Briggs v. Spaulding, 141 U. S. 132, 162.

[2] Wakeman v. Dalley, 51 N. Y. 27, 32.

[3] Hallmark's Case, L. R. 9 Ch. Div. 329.

known the contents of all the books and documents of the company, and so to have known that his name was on the register of shares for fifty shares. But he swears that in fact he did not know that any shares had been allotted to him. Is knowledge to be imputed to him under any rule of law? As a matter of fact no one can suppose that a director of a company knows everything which is entered in the books; and I see no reason why knowledge should be imputed to him which he does not possess in fact. Why should it be his duty to look into the list of shareholders? I know no case except Ex parte Brown,[1] which shows that it is the duty of a director to look at any of the entries in the books; and it would be extending the doctrine of constructive notice far beyond that or any other case to impute to this director the knowledge which it is sought to impute to him in this case."

A principal stockholder in a corporation who knew that a person was employed by it as its president was held bound by the contents of its corporate books in respect of his salary when they were open to her examination and she failed to make an examination within a reasonable time.[2]

§ 517. **Liability for care of papers.**—The liability of the officers of a corporation for corporate funds and papers intrusted to their care is that of an ordinary trustee or bailee for hire.[3]

§ 518. **Liability for mistakes.**—Directors are not liable for mistakes of fact if they exercise due diligence and care. Thus they are not personally liable for erroneously paying a dividend out of capital if they made a careful investigation and honestly believed that there were profits out of which to pay the dividend.[4] So where the directors act in good faith and with proper diligence, they are not responsible for mistakes of law.[5] They are not bound to consult counsel,[6] and the fact

[1] 19 Beav. 97.

[2] Church v. Cementico Co. (Minn.), 77 N. W. Rep. 548.

[3] Mowbray v. Antrin (Ind.), 23 N. E. Rep. 858.

[4] Excelsior, etc., Co. v. Lacey, 63 N. Y. 422.

[5] Hodges v. New England, etc., Co., 1 R. I. 312, 53 Am. Dec. 624; Williams v. McDonald, 37 N. J. Eq. 409; Spering's Appeal, 71 Pa. St. 11, 10 Am. Rep. 684.

[6] Vance v. Phœnix, etc., Co., 4 Lea (Tenn.) 385.

of having consulted counsel, while evidence of care, will not necessarily exempt them from liability if they do not act in good faith.[1]

§ 519. **Liability on contracts.**[2]—The liability of the officer or agent of a corporation on a contract made by him on behalf of the corporation is governed by the general principles of the law of agency, and not by any principles peculiar to the law of corporations. If the agent exceeds his authority, he is himself liable upon the contract.[3] It has been held that the agent is liable in contract when he acts in good faith, and in tort when he acts in bad faith; that he is liable on an implied warranty of authority;[4] and that the liability is in all cases in tort.[5] A person who acts as the agent of a foreign corporation which is not authorized to do business in the state, knowing such to be the fact, is personally liable on the contract.[6]

§ 520. **Liability to third persons for torts.**—An officer of a corporation who, in the course of his employment, is guilty of a tort, is personally liable to the person injured for the damages caused thereby, notwithstanding the fact that the corporation may also be liable.[7] But it must appear that the act was committed by such officer, or that it was his duty to attempt to prevent it, and that he failed to do so.[8] Thus, the manager of a corporation in charge of its works is personally liable for damages because of his negligent failure to erect a

[1] See Caulkins v. Gas Light Co., 85 Tenn. 683, 4 Am. St. Rep. 786.

[2] See Wilgus' Cases, Relation of Officers to Dealers and Non-Dealers.

[3] See note to 53 Am. Dec. 649; Kroeger v. Pitcairn, 101 Pa. St. 311, 47 Am. Rep. 718; Feeter v. Heath, 11 Wend. (N. Y.) 478; Keener v. Harrod, 2 Md. 63.

[4] Farmers', etc., Co.v. Floyd, 47 Ohio St. 525; Nelligan v. Campbell, 20 N. Y. Supp. 234; Lasher v. Stimpson, 145 Pa. St. 30; Lewis v. Tilton, 64 Iowa 220, 19 N. W. Rep. 911.

[5] Jefts v. York, 10 Cush. (Mass.) 392.

[6] Lasher v. Stimpson, 145 Pa. St. 30.

[7] As to liability for misrepresentation as to solvency of the corporation, see Houston v. Thornton, 122 N. C. 365, 65 Am. St. Rep. 699 and note, p. 707. See, also, notes to 8 Am. St. Rep. 604 and 48 Am. St. Rep. 921, 7 Am. Dec. 255.

[8] Nunnelly v. Southern, etc., Co., 94 Tenn. 397, 28 L. R. A. 421, annotated; Cameron v. Kenyon-Connell, etc., Co. (Mont.), 44 L. R. A. 508; People v. England, 27 Hun (N. Y.) 139.

scaffold which is necessary for the protection of persons passing near the building.[1] So, an officer and general manager of a lumber company is personally liable for setting an inexperienced and ignorant employe at work upon dangerous machinery without giving him proper instructions.[2] The officers of a mining company are personally liable for damages caused to a riparian proprietor by the long-continued discharge of muddy water into a stream with their knowledge and consent.[3] The directors are liable to a person who, by fraudulent representation made by the directors, are induced to contract with a corporation to their injury. Such an act is founded upon the personal tort of the directors.[4] A purchaser of mortgage bonds issued by a corporation who relies upon a statement on their face that they are first mortgage bonds, may recover the damages sustained thereby from the corporate officers who issued the bonds with the intention that the statement should be acted on as true by the purchaser.[5] Officers and directors who knowingly issue or cause to be issued a prospectus containing false statements of material facts, which have a natural tendency to mislead, are liable personally to persons who purchase the corporate stock in reliance thereon.[6] Such a case must, of course, come within the general rules governing other actions for false representation.[7]

§ 521. **Violation of charter or statute.**—The liability of an officer for neglect of the duty which he owes to the corporation does not rest upon the fact that the act is prohibited by statute, but upon the violation of a common law duty. Thus Morawetz says:[8] The liability of directors for damages caused

[1] Mayer v. Thompson, etc., Co., 104 Ala. 611, 28 L. R. A. 433.

[2] Greenberg v. Whitcomb, etc., Co., 90 Wis. 225, 28 L. R. A. 439.

[3] Nunnelly v. Southern, etc., Co., 94 Tenn. 397, 28 L. R. A. 421.

[4] Salmon v. Richardson, 30 Conn. 360.

[5] Bank of Atchison Co. v. Byers, 139 Mo. 627.

[6] Morgan v. Skiddy, 62 N. Y. 319. See § 370.

[7] Cole v. Cassidy, 138 Mass. 437.

[8] Morawetz Priv. Corp., § 556, quoted with approval in Briggs v. Spaulding, 141 U. S. 132. See also North Hudson, etc., Assn. v. Childs, 86 Wis. 292.

by acts expressly prohibited by the company's charter or act of incorporation is not created by force of the statutory prohibition. The performance of acts which are illegal or prohibited by law may subject the corporation to a forfeiture of its franchises and the directors to criminal liability; but this would not render them civilly liable for damages.[1] The liability of directors to the corporation for damages caused by unauthorized acts rests upon the common law rule which renders every agent liable, who violates his authority to the damage of his principal. A statutory prohibition is material under these circumstances, merely as indicating an express restriction placed upon the powers delegated to the directors when the corporation was formed.

§ 522. **Liability imposed by statute.**—The officers and directors of a corporation are, by statute, in some states made liable for the debts of the corporation. The liability is sometimes absolute to a certain amount,[2] or for an amount in excess of a designated indebtedness,[3] but more commonly it is penal for a breach or neglect of duty,[4] as a failure to make a report,[5] or the making of a false report,[6] or violating any of the provisions of the act under which the corporation is incorporated whereby it becomes insolvent.[7] Such statutes are strictly construed, and under them a clear case must be made out in order to render the officer liable.[8]

[1] But see Baxter v. Coughlan (Minn.), 72 N. W. Rep. 797.

[2] State Bank v. Andrews, 18 N. Y. Supp. 167.

[3] Thatcher v. King, 156 Mass. 490; Tradesman's, etc., Co. v. Knoxville, etc., Co., 95 Tenn. 634, 31 L. R. A. 593.

[4] Patterson v. Minnesota, etc., Co., 41 Minn. 84.

[5] Gold v. Clyne, 134 N. Y. 262, 31 N. E. Rep. 980, 17 L. R. A. 767; Bank v. Pierson, 112 Mich. 410.

[6] Torbett v. Godwin, 62 Hun 407; Ferguson v. Gill, 19 N. Y. Supp. 149; Chittenden v. Thannhauser, 47 Fed. Rep. 410; Pier v. Hanmore, 86 N. Y. 95; Matthews v. Patterson, 16 Colo. 215. Paying a dividend out of capital. Korke v. Thomas, 56 N. Y. 559.

[7] Patterson v. Minnesota, etc., Co., 41 Minn. 84; Clow v. Brown, 150 Ind. 185.

[8] Garrison v. Howe, 17 N. Y. 458; Bruce v. Platt, 80 N. Y. 379. The statute of limitation governing penalties applies. Merchants' Bank v. Bliss, 35 N. Y. 412. In Jones v. Barlow, 62 N. Y. 202, it was held that the statute begins to run from the time when the cause of action accrues to the creditor, and not from the time of the default in making the report.

The failure by the directors of a corporation to file an annual report of its assets and liabilities, as required by the statute, will not render them personally liable for a contingent liability of the corporation under an executory contract, which does not become an existing debt until the corporation has expired by the terms of its articles of incorporation.[1] It is essential to the liability of directors for default in filing a report that their occupancy of that relation, that such default, and that the debt of the corporation, have existence at the same point of time.[2] The liability of the directors dependent on default in filing a report is measured by the obligation of the company and the remedy against it and them is concurrent.[3] The report need not be made after the corporation has ceased to have a legal existence. After the death of the company, it could make no report, and the directors are not chargeable with liability founded upon such omission. It has been held that even after a *de facto* dissolution no report is necessary for the protection of the directors.[4] But the mere fact that the corporation has ceased to do business does not excuse the failure to file the report.[5] A creditor who seeks to hold a director liable for the failure to file a report must show that he is a creditor, and the fact that he has obtained judgment is prima facie evidence that he is a creditor.[6] A director will not be permitted to profit by his own wrong, and, hence, neither a director who is a creditor nor his assignee can maintain an action against the other directors for a breach of duty of which he is also guilty.[7] No vested right can be acquired in a penalty, and, therefore, statutes of this character which impose liability upon the direct-

[1] Gold v. Clyne, 134 N. Y. 262, 17 L. R. A. 767.

[2] Shaler, etc., Co. v. Bliss, 27 N. Y. 297; Duckworth v. Roach, 81 N. Y. 49.

[3] Jones v. Barlow, 62 N. Y. 202; Trinity Church v. Vanderbilt, 98 N. Y. 170.

[4] Huguenot Bank v. Studwell, 74 N. Y. 621; Bonnell v. Griswold, 80 N. Y. 128; Gold v. Clyne, 134 N. Y. 262, 17 L. R. A. 767. For the effect of a failure to file a report, as subjecting the corporation to forfeiture of its charter, see People v. Buffalo, etc., Co., 131 N. Y. 140, 15 L. R. A. 240.

[5] Sanborn v. Lefferts, 58 N. Y. 179. See International Bank v. Faber, 86 Fed. Rep. 443, 57 U. S. App. 153.

[6] Miller v. White, 50 N. Y. 137.

[7] Knox v. Baldwin, 80 N. Y. 610. The liability may be enforced by a creditor stockholder. Sanborn v. Lefferts, 58 N. Y. 179.

ors may be repealed and the right of action taken away at any time before judgment is entered.[1] Where a statute makes the directors personally liable when they consent to the creation of indebtedness in excess of the assets of the corporation, it must be shown that the consent was given in the capacity of a director. The term indebtedness, in such connection, includes bonded indebtedness. The liability is for the benefit of creditors whose debts were thus illegally contracted, and must be enforced by a bill filed for the benefit of all creditors similarly situated.[2]

§ 523. **Liability of directors where corporation maintains a nuisance.**—It is the duty of the directors of a corporation to avoid the creation of nuisances by their corporation through its employes acting within the line of their duty. The nonperformance of this duty, which results in the creation and maintenance of a continuing nuisance by the corporation which causes the death of a third person, amounts to a misfeasance on their part, or of malfeasance, if they have actual knowledge of and authorized the nuisance. Where the tort has been committed through the directors, they can not escape liability by showing that they acted in a vicarious character.[3] In an action against the directors of a corporation to recover damages for personal injury occasioned by the explosion of giant powder kept by the corporation within the city limits in violation of law, the court said:[4] "The corporation therefore,

[1] Knox v. Baldwin, 80 N. Y. 610; Gregory v. Bank, 3 Colo. 332.

[2] Tradesman's, etc., Co. v. Knoxville, etc., Co., 95 Tenn. 634, 31 L. R. A. 593.

[3] The liability of a director in tort is not to be avoided by his "vicarious character" where the tort of a corporation has been committed through the director. Nunnelly v. Southern, etc., Co., 94 Tenn. 397, 28 L. R. A. 421; Bank v. Byers, 139 Mo. 627; Delaney v. Rochereau & Co., 34 La. An. 1123, 44 Am. Rep. 456. The relation of contract to a corporation neither adds to nor subtracts from a man's duty to strangers to so use his own property or that under his control as not to injure another. Baird v. Shipman, 132 Ill. 16, 7 L. R. A. 128; note to Nunnelly v. Southern, etc., Co., 28 L. R. A. 421; Jenne v. Sutton, 43 N. J. L. 257, 39 Am. Rep. 578; Mayer v. Thompson, etc., Co., 104 Ala. 611, 28 L. R. A. 433.

[4] Cameron v. Kenyon-Connell, etc., Co. (Mont.), 56 Pac. Rep. 358, 44 L. R. A. 508, and extensive note on liability of the officers of a corporation for the torts or negligence of the corporation.

by maintaining this nuisance became subject to indictment for misdemeanor as well as liable in a civil action for injury to persons or property caused by the nuisance.[1] * * * As said before, the trustees manage the stock, property and concerns of the corporation; wherefore it is difficult to see how all responsibility in this management can be avoided as long as the trustees hold their offices. Certainly the ministerial work in a corporation can be delegated to subordinate agents, and often must be. The details of a corporation's business necessitates this; and if directors act in good faith and with reasonable care and diligence in appointing and supervising such inferior agents they are not personally responsible for damages occasioned by the agents' negligence or even crime. But a director can not wholly escape his duty of supervision or transfer his authority to represent his principal at least without the principal's consent. Otherwise he could evade every responsibility imposed by law upon him by simply absenting himself from meetings, or by avoiding information of the acts of the other directors in expressing the will of the corporation or by delegating an employe to act as trustee for him.[2] * * *

Third persons may hold directors liable in positive tort, upon the principal that a positive wrong done by a servant or ordinary agent must be applied to the misfeasance of directors also.[3] * * * It is therefore the duty of the trustees of a corporation dealing in explosives to exercise such reasonable supervision over the management of their company's business as will result in the observance of the utmost care on the part of the subordinates who directly handle the explosives. This rule grows out of the great principle of social duty that every man in the management of his own affairs, whether by himself or by his agents or servants, shall so conduct them as not to injure another; and if he does not, and another thereby sustains damage, he shall answer for it.[4] It is likewise their duty to avoid the creation of nuisances by their corporation

[1] Heeg v. Licht, 80 N. Y. 579, 36 Am. Rep. 654.

[2] Morawetz Priv. Corp., § 536.

[3] Salmon v. Richardson, 30 Conn. 360, 79 Am. Dec. 255.

[4] Farwell v. Boston, etc., Corp., 4 Metc. (Mass.) 49, 38 Am. Dec. 339.

through its employes acting within the line of their duties. Nor will inaction of itself overthrow the force of this obligation upon trustees to so control their corporation's business as to not negligently injure third persons. Along with the assumption of the duties of trusteeship go the duties of exercising reasonable care in the manner of performing those duties. This reasonable care appears not to have been exercised in this case where the corporation by its trustees permitted a public nuisance to be created, and to continue, whereby, as a consequence of the act of permitting it, a third person not in fault has been killed. Because directors are themselves agents, it is none the less true that they owe a common law duty to third persons. If they violate that duty they are responsible, whether the violation is the result of a wrongful omission or commission."[1]

§ 524. **Liability imposed for benefit of third persons.**—In some states there are statutes which impose upon the directors and managing officers of corporations a liability for the benefit of third persons who are injured by some forbidden act or negligence of the officer.[2] Where a statute prohibits the doing of an act or imposes a duty upon one for the protection and benefit of individuals, if he disobeys the prohibition or neglects to perform the duty, he is liable to those for whose protection the statute was enacted for any damages resulting proximately from such disobedience or neglect. Where a statute made it a criminal offense for an officer or director of any bank to accept deposits of money when he knows or has good reason to know that the bank is unsafe or insolvent, the court said:[3] "The purpose of this statute is to protect depositors in a bank by punishing its officers for receiving deposits when the bank is insolvent. By necessary implication it makes it the duty of the directors or other officers of the bank to refrain from accepting or receiving deposits when they know the bank to be insolvent. The solvency or insolvency of a bank is a matter

[1] Mechem Agency, § 572.

[2] See Bruce v. Platt, 80 N. Y. 379; Pier v. Hanmore, 86 N. Y. 95.

[3] Baxter v. Coughlin (Minn.), 72 N. W. Rep. 797. See Bishop Non-Contract Law, § 132; Cooley Torts, p. 780; Bott v. Pratt, 33 Minn. 323; Osborn v. McMasters, 40 Minn. 103.

peculiarly within the knowledge of its directors. On the other hand, depositors have no means of accurately informing themselves on the subject. They must act on the presumption that directors are not violating the law by keeping their bank open to receive deposits when it is insolvent. This case falls then within the rule that where the statute prohibits the doing of an act, or imposes a duty on one for the benefit and protection of individuals, if he disobeys the prohibition or neglects to perform the duty, he is liable to those for whose protection the statute was enacted for any damages resulting proximately from such disobedience or neglect."

§ 525. **Remedy of the corporation against an officer.**—Where a corporation has been damaged by the fraud or negligence of one of its officers or agents, it may proceed against him in an action for damages, or for an accounting in equity.[1] Ordinarily the action must be brought in the name of the corporation, although, as has been explained elsewhere, an action of this character may be maintained by an individual stockholder under certain circumstances.

§ 526. **Statute of limitations.**—The statute of limitations does not run against the claim of a corporation against an officer for misappropriation of corporate funds, as the relation is one of trust.[2]

§ 527. **No liability to corporate creditors.**—The liability of an officer for mismanagement, fraud or negligence, which causes loss to the corporation, is to the corporation and not to its creditors, but the claim against the officer forms a part of the assets of the corporation and may be reached by the creditors in a proper proceeding. The right is sometimes based upon the trust-fund theory, and sometimes upon the general rule that the creditors have the right to reach the equitable

[1] Horn, etc., Co. v. Ryan, 42 Minn. 196; Robinson v. Smith, 3 Paige (N. Y.) 222, 24 Am. Dec. 212; Hodges v. Screw Co., 1 R. I. 312, 53 Am. Dec. 624.

[2] Ellis v. Ward, 137 Ill. 509, 25 N. E. Rep. 530. Approved in 3 Thompson Corps., § 4128. *Contra*, Williams v. Halliard, 38 N. J. Eq. 373. See Wallace v. Lincoln, etc., Bank, 89 Tenn. 630, 24 Am. St. Rep. 625. See, also, In re Lands, etc., Co., L. R. (1894) 1 Ch. 616; 7 Eng. R. Cas. 614, with English and American notes.

assets of the corporation, and to have them applied to the satisfaction of their claim.[1] An action at law can not be maintained by a creditor against an officer whose wrongful conduct has resulted in injury to the corporation.[2] But after the corporation has become insolvent the creditor who has recovered judgment against the corporation may proceed against the officer.[3] The proper proceeding is by way of a creditor's bill.[4]

§ 528. **Powers of particular officers.**[5]—The powers of corporate officers are such as are conferred upon them by the terms of their agency. It may be expressly conferred by charter, by-laws, or a resolution, or implied from the nature of the office, and the duties ordinarily devolving upon such officers, or agents. The duties and powers commonly granted to such officers as president, secretary and treasurer are well understood, and within the scope of this apparent authority the officer acts for the corporation and can bind it by contracts made in its name. Within the line of his ordinary duties, such an officer requires no express authority.[6] After citing many decisions in support of the general propositions, Mr. Cook says:[7] "These decisions show that a corporation is bound by its agents' acts only when a partnership would be bound under similar circumstances, and in general a corporation may ratify and adopt the unauthorized acts of its agents. There are no arbitrary rules as to the mode of making a corporate contract. A contract may be inferred from corporate acts and customs without a vote or formal act. It is not necessary that such

[1] Morawetz Priv. Corp. 2, § 795.

[2] Zinn v. Mendel, 9 W. Va. 580; Smith v. Poor, 40 Me. 415.

[3] Gratz v. Redd, 4 B. Mon. (Ky.) 178; Ellis v. Ward, 137 Ill. 509; Wilkinson v. Bauearle, 41 N. J. Eq. 635.

[4] Schley v. Dixon, 24 Ga. 273.

[5] See Wilgus' Cases, Louisville, etc., R. Co. v. McNay, 98 Ind. 391.

[6] See, generally, Jones v. Williams, 139 Mo. 1, 61 Am. St. Rep. 437, annotated. Bank v. Dunn, 6 Pet.(U. S.) 51. A director of a corporation is not an agent in the sense that he can bind it by contract. Limer v. Traders Co., 44 W. Va. 175; Allemong v. Simmons, 122 Ind. 199. See Woodbury, etc., Co. v. Mulliken & Gibson, 66 Vt. 465, and Gaynor v. Williamsport, etc., R. Co., 189 Pa. St. 5, 41 Atl. Rep. 978. Parties contracting with officers of a corporation must ascertain the scope of their authority. Des Moines, etc., Co. v. Tilford, etc., Co. (Iowa), 70 N. W. Rep. 839.

[7] Cook Priv. Corp., § 720, citing many cases.

assent and acceptance should be under seal and in writing or be spread upon the records. The acceptance of the consideration of an unauthorized contract by the corporation, however, without knowledge of the terms of the contract or of the account upon which it is paid is not in itself a ratification of the contract."

§ 529. **The president.**—The president of a corporation derives his authority from the power which elects him. This is ordinarily the board of directors. He has no authority by virtue of his office to control or dispose of the property of the corporation. He can not act or contract for the corporation, without express authority, to any greater extent than any other director. By the great weight of authority, "a president has no inherent power to represent or contract for the corporation. His duties are confined to presiding and voting as a director. The fact, however, that he is almost always the corporate officer who is directed to sign the corporate contracts that have been authorized by the board of directors has led to the enlargement of his importance as a corporate officer. Hence the rule has arisen in New York that a contract which is apparently a corporate contract, being duly signed by the president, is presumed to be a corporate contract until the want of authority is shown by the corporation."[1] Authority to do a particular act may be shown by the fact that the same or similar acts have frequently been done by the officer with the knowledge of the corporation.[2] The president may of course bind the

[1] Cook Priv. Corp., § 716; Potts v. Wallace, 146 U. S. 689; Brush, etc., Co. v. Montgomery (Ala.), 21 So. Rep. 960. In Titus v. Cairo, etc., R. Co., 37 N. J. L. 98, the court said: "In the absence of anything in the act of incorporation bestowing special power upon the president, he has from his official station no more control over the corporate property and funds than any other director." See, also, as to powers of president, Pacific Bank v. Stone, 121 Cal. 202; White v. Taylor, 113 Mich. 543; Main v. Casserly, 67 Cal. 127. As to the powers of a general manager, see Helena Nat. Bank v. Rocky, etc., Co., 20 Mont. 379, 63 Am. St. Rep. 628; Thayer v. Nehalem, etc., Co., 31 Ore. 437, 51 Pac. Rep. 202; Butte, etc., Co. v. Montana, etc., Co. (Mont.), 55 Pac. Rep. 112. See, generally, notes to 14 L. R. A. 356, 61 Am. St. Rep. 459.

[2] Swasey v. Emerson, 168 Mass. 118. That long usage may confer authority, see Estes v. German Nat'l Bank, 62 Ark. 7; Missouri, etc., R. Co. v. Sidell, 67 Fed. Rep. 464.

corporation by contracts when authorized to do so by the board of directors,[1] and the authority to do so may be implied from a long course of acquiescence on the part of the directors,[2] as where, with the knowledge and consent of the directors, the president has for a long period practically conducted the entire business of the corporation.[3] The president of a corporation has no implied power to direct the treasurer to refuse payment of a subscription,[4] to employ an architect,[5] to execute a mortgage in the name of the corporation,[6] even when he has been given power to pledge notes and contracts,[7] to execute notes in the name of the corporation,[8] to confess judgment for the corporation,[9] to assign a patent-right in payment of a corporate debt,[10] to sell treasury stock,[11] to negotiate a loan for the corporation and pay a large brokerage commission,[12] to make a contract increasing the price of construction work,[13] to agree that sureties on a note shall not be bound,[14] to borrow money for the corporation,[15] to release a claim in favor of the corporation,[16] to sell

[1] Castle v. Belfast, etc., Co., 72 Me. 167; Baker v. Cotter, 45 Me. 236.

[2] Fitzgerald, etc., Co. v. Fitzgerald, 137 U. S. 98; Martin v. Niagara Falls, etc., Co., 122 N. Y. 165.

[3] G. V. B. Mining Co. v. Nat. Bank (C. C. App.), 95 Fed. Rep. 23; Senour, etc., Co. v. Clarke, 96 Wis. 469; McComb v. Barcelona, etc., Assn., 134 N. Y. 598; Fifth Nat'l Bank v. Navassa, etc., Co., 119 N. Y. 256; Sherman, etc., Co. v. Morris, 43 Kan. 282. The management of the business may be entrusted to the president, either by an express resolution of the board of directors, or by their acquiescence in a course of dealing. Jones v. Williams, 139 Mo. 1, 37 L. R. A. 682.

[4] Potts v. Wallace, 146 U. S. 689.

[5] Wait v. Nashua, etc., Assn. (N. H.), 23 Atl. Rep. 77; Mathias v. White, etc., Assn. (Mont.), 48 Pac. Rep. 624.

[6] Alta, etc., Co. v. Alta, etc., Co., 78 Cal. 629; National State Bank v. Vigo, etc., Bank, 141 Ind. 352; England v. Dearborn, 141 Mass. 590.

[7] Currie v. Bowman, 25 Ore. 364.

[8] Estes v. German, etc., Bank, 62 Ark. 7; Edwards v. Carson, etc., Co., 21 Nev. 469.

[9] Raub v. Balirtown, etc., Assn., 56 N. J. L. 262; Ford v. Hill, 92 Wis. 188.

[10] Kansas, etc., Co. v. DeVol, 72 Fed. Rep. 717.

[11] In re Utica, etc., Co., 154 N. Y. 268, 48 N. E. Rep. 521.

[12] Tobin v. Roaring, etc., R. Co., 86 Fed. Rep. 1020.

[13] Grant v. Duluth, etc., R. Co., 66 Minn. 349, 69 N. W. Rep. 23.

[14] Bank v. Bennett, 33 Mich. 520; Bank v. Tisdale, 84 N. Y. 655.

[15] Life, etc., Co. v. Mech., etc., Co., 7 Wend. (N. Y.) 31; Western Nat'l Bank v. Armstrong, 152 U. S. 346.

[16] Olney v. Chadsey, 7 R. I. 224; Rhodes v. Webb, 24 Minn. 292. See Indianapolis, etc., Co. v. St. Louis, etc., R. Co., 120 U. S. 256.

and assign notes held by the corporation bank,[1] to bind a national bank by a purchase of bonds and stock for it,[2] to let a railroad construction contract,[3] to sell property belonging to the corporation, unless he has made similar contracts before, without objection,[4] to issue drafts in the name of the corporation,[5] to execute accommodation paper,[6] to agree on its behalf with a person who sells it property to be paid for in stock, to repurchase the stock if he becomes dissatisfied with it.[7] The president may employ an attorney for the corporation;[8] but may not commence an action.[9] But it has been held that he has no power to employ an attorney,[10] although the general officers and manager may employ an attorney to represent the bank in all matters growing out of the general business of the corporation.[11] A corporation may of course ratify the acts of the officer by accepting and retaining the benefits of his act.[12] The powers of the president of a corporation have been somewhat extended by the Illinois courts, where it is held that he has power to agree that an absolute subscription may be changed to a conditional subscription in such a way as to estop himself, and creditors and stockholders, with knowledge of the facts un-

[1] Hollowell, etc., Bank v. Hamlin, 14 Mass. 178.

[2] First Nat'l Bank v. Hoch, 89 Pa. St. 324.

[3] Templin v. Chicago, etc., R. Co., 73 Iowa 548; Griffith v. Chicago, etc., R. Co., 74 Iowa 85.

[4] Pittsburg, etc., Co. v. Reese, 118 Pa. St. 355.

[5] Dabney v. Stevens, 40 How. Pr. (N. Y.) 341.

[6] McLellan v. Detroit, etc., Works, 56 Mich. 579.

[7] Olds v. Phillipsburg, etc., Co. (Tenn.), 48 S. W. Rep. 285.

[8] American, etc., Co. v. Oakley, 9 Paige (N. Y.) 496; Mumford v. Hawkins, 5 Denio 355; Davis v. Memphis, etc., R. Co., 22 Fed. Rep. 883; Dallas, etc., Co. v. Crawford (Tex.), 44 S. W. Rep. 875.

[9] Ashuelot, etc., Co. v. Marsh, 55 Mass. 507. *Contra*, Lucky, etc., Co. v. Abraham, 26 Ore. 282. That the president may bring a writ of entry to foreclose a mortgage, see Trustees, etc., v. Connolly, 157 Mass. 272. The president, in the exercise of his inherent power to take charge of the litigation of the bank, may assign a judgment to a trustee in order that an action may be brought for its collection. Guernsey v. Black, etc., Co., 99 Iowa 471.

[10] Pacific Bank v. Stone (Cal.), 53 Pac. Rep. 634.

[11] Lewis v. Publishing Co., 77 Mo. App. 434.

[12] Wells v. St. Paul, etc., Co., 63 Minn. 370; Scott v. Middleton, etc., R. Co., 86 N. Y. 200; Omaha, etc., Co. v. Burns, 49 Neb. 229.

der certain conditions,[1] to execute a note for the corporation,[2] to sign a chattel mortgage in the name of the corporation,[3] or to contract for transportation of railroad iron.[4] The president and general manager of an insurance company may bind it by a contract that its mortgagor may have a certain time within which to redeem from a foreclosure sale.[5]

§ 530. **The vice-president.**—The rules which govern the powers and conduct of the president of a corporation apply also to the vice-president.[6] Unless otherwise provided by statute, the charter or by-laws of the corporation, the deed of the corporation may be executed as well by the vice-president as by the president. And when so executed with the necessary formalities, it will be presumed that the vice-president had authority to act on behalf of the corporation.[7]

§ 531. **The secretary.**—The secretary ordinarily represents the corporation in the conduct of its routine business, but his authority, like that of all other officers, is derived from the terms of his employment. He has no inherent power by virtue of his office to make contracts for the corporation.[8] He is

[1] Morgan Co. v. Thomas, 76 Ill. 120.

[2] Matson v. Alley, 141 Ill. 284; Snyder Bros. v. Bailey (Ill.), 46 N. E. Rep. 452.

[3] Anderson v. South Chicago, etc., Co. (Ill.), 50 N. E. Rep. 655.

[4] Chicago, etc., R. Co. v. Coleman, 18 Ill. 297.

[5] Union, etc., Co. v. White, 106 Ill. 67. The president and business manager of a corporation has no implied power to create an indebtedness against it by assuming for it liability for an individual debt of his own, without a just consideration to the corporation. Barnhardt v. Star Mills (N. C.), 31 S. E. Rep. 719. In Lamson v. Beard (C. C. App.), 94 Fed. 30, it was held that when the president of a bank draws drafts upon the funds of the bank to pay his personal debts, the drawee is put upon inquiry as to his authority. As to implied authority of president, see Sparks v. Dispatch Transfer Co., 104 Mo. 531, 24 Am. St. Rep. 351, and note 24 Am. St. Rep. 137.

[6] See, generally, as to the powers of a vice-president, Missouri, etc., Co. v. Faulkner, 88 Tex. 649; Cox v. Robinson, 82 Fed. Rep. 277; Smith v. Smith, 62 Ill. 493; Huse v. Ames, 104 Mo. 91; Dallas v. Columbia, etc., Co., 158 Pa. St. 444; Streeten v. Robinson, 102 Cal. 542.

[7] Ellison v. Brandstrator (Ind.), 54 N. E. Rep. 433. Citing Smith v. Smith, 62 Ill. 493; Colman v. Land Co., 25 W. Va. 148; Bowers v. Hechtman, 45 Minn. 238; Shaffer v. Hahn, 111 N. C. 1.

[8] Wolf Gaines v. Davenport, etc., R. Co., 93 Iowa 218; Read v. Buffum, 79 Cal. 77, 12 Am. St. Rep. 131. In the discharge of his ordinary duties the secretary represents the corporation. Hastings v. Brooklyn, etc., Co., 138 N. Y. 473.

the proper custodian of the corporate seal, and when he affixes it to a deed or other instrument, the presumption is that he did it by the direction of the corporation, and it devolves upon those who dispute the validity of the instrument to prove that he acted without authority.[1]

§ 532. **The treasurer.**—The treasurer is the general fiscal agent of the corporation and is commonly given powers in the management of its financial matters. But he has no power by virtue of his office alone to borrow money and give the corporate notes therefor.[2] The authority to sign notes on behalf of the corporation need not appear in the by-laws, nor need it have been expressly given by a vote of the directors or stockholders. It may be inferred from usage, and will be implied when he has been accustomed to act as the managing agent of the corporation.[3] But if the corporation permits the treasurer to act as its general fiscal agent, and holds him out to the public as having the general authority implied from his official name and character and by its silence and acquiescence allows him to draw and accept drafts and sign and endorse notes, it is bound by his acts when done within the scope of such apparent authority.[4] The question is also affected by the character of the business transacted by the corporation. Thus, in a recent case it was held that the treasurer of a gas light company had au-

[1] Ellison v. Brandstrator (Ind.), 54 N. E. Rep. 433. The secretary can not bind the corporation for the price of goods ordered by him from another corporation with which he is connected. Stillwell, etc., Co. v. Niles, etc., Co. (Mich.), 72 N. W. Rep. 1107.

[2] Craft v. South Boston, R. Co., 150 Mass. 207, 5 L. R. A. 641; 22 N. E. Rep. 920; Appeal of Philler, 161 Pa. St. 157; In re Millward-Cliff, etc., Co. (Pa.), 28 Atl. Rep. 1072; Fifth Ward Sav. Bank v. First Nat'l Bank, 48 N. J. L. 513; Chemical, etc., Bank v. Wagner, 93 Ky. 525, 20 S. W. Rep. 535; Page v. Fall River, etc., R. Co., 31 Fed. Rep. 257; Lester v. Webb, 1 Allen 34. See also Glidden, etc., Co. v. Bank, 69 Fed. Rep. 912, 32 U. S. App. 654; Grommes v. Sullivan, 81 Fed. Rep. 45, 53 U. S. App. 359. As to power to endorse paper for discount and sale, see Blake v. Domestic, etc., Co. (N. J.), 38 Atl. Rep. 241.

[3] Chicago, etc., Co. v. Chicago Nat'l Bank, 176 Ill. 224.

[4] Merchants Nat'l Bank v. Citizens, etc., Co., 159 Mass. 505; McNeil v. Boston Chamber of Com., 154 Mass. 277; Mining Co. v. Anglo-Cal. Bank, 104 U. S. 192; Credit Co. v. Howe, etc., R. Co., 54 Conn. 357; Page v. Fall River, etc., Co., 31 Fed. Rep. 257; Blake v. Domestic, etc., Co. (N. J.), 38 Atl. Rep. 241; Case Mfg. Co. v. Soxman, 138 U. S. 431.

thority by virtue of his office to sign a promissory note which would bind the corporation. The court said: "Upon consideration of the decisions cited, we think it fair to say that the making and endorsing of negotiable paper is to be presumed to be within the power of the treasurer of a manufacturing and trading corporation, whenever, from the nature of its ordinary business as usually conducted, the corporation is naturally to be expected to use its credit in carrying on its commercial transactions. Such paper is the usual and ordinary instrument of utilizing credit in commercial dealings, and it is for the interest of the corporation and of the community that the best instrument should be employed. It is no less for the interest of all that, if negotiable paper is to be employed, its validity should not be open to objections which would impair its usefulness by requiring at every step an inquiry into the authority by which it is issued."[1]

§ 533. **De facto officers.**—The injustice which would result from requiring those who are obliged to deal with corporations to investigate and decide who are rightfully exercising the functions of a corporate office, and the great inconvenience of litigating the title to such offices in collateral proceedings, has led to the adoption of the rule that he who publicly exercises the functions of such an office, not in a single instance only but continuously, will be treated as a *de facto* officer and his acts upheld as against third persons and the corporation.[2]

[1] Merchants Nat'l Bank v. Citizens, etc., Co., 159 Mass. 505; Matson v. Alley, 141 Ill. 284. The treasurer of a water-works company has no implied power to borrow money. First Nat'l Bank v. Council Bluffs, etc., Co., 9 N. Y. Supp. 859. As to powers of treasurer in other respects see Jackson v. Campbell, 5 Wend. 571; Dedham Inst. v. Slack, 6 Cush. 408; Brown v. Winnisimmet, 93 Mass. 326; Perkins, etc., Co., v. Bradley, 24 Vt. 66; State v. Felton (N. J.), 19 Atl. Rep. 123; Alexander v. Cauldwell, 83 N. Y. 480; Phillips v. Campbell, 43 N. Y. 271; Adams v. Mills, 60 N. Y. 533; Odd Fellows v. Bank, 42 Mich. 461; Stevens v. Carp River, etc., Co., 57 Mich. 427; Kalamazoo, etc., Co. v. McAlister, 36 Mich. 327; Tripp v. New, etc., Co., 137 Mass. 499.

[2] Hamm v. Drew, 83 Tex. 77; Cahill v. Kalamazoo, etc., Co., 2 Doug. (Mich.), 124, 43 Am. Dec. 457. Note in 19 Am. and Eng. Corp. Cas. 160. As to the application of the same principle to officers of public corporation, see Elliott Pub. Corps., § 265, and cases there cited. See, also, note to L. R. A. 418.

It is only necessary for a person, who deals with a corporation, "to inquire what power directors of the corporation have and what acts the corporation has authorized them to do. They are not required to investigate the qualifications which the corporation has prescribed to itself, as the condition upon which any one should be elected a director or permitted to act as such. The corporation and not the general public have the means of knowing whether a director, whom they have elected as such, is qualified to act as a director, according to their by-laws. If he is not qualified at the time of his election, it is within their power to require him either to possess himself of the requisite qualifications, or else to proceed to another election. If, instead of doing this, they leave his election as a director upon record, as though he were at law eligible, and thus hold him out and permit him to hold himself out as a director, and he acts as such, they are bound by his acts as fully as though he were properly qualified."[1] A person exercising the functions of a director, but who was elected at a meeting held in another state, is a *de facto* director.[2] A contract made by *de facto* officers binds the corporation.[3]

§ 534. **Notice to officers and agents.**[4]—An officer or agent of a corporation represents the corporation when he is acting within the scope of his duties, and his knowledge acquired while so engaged with reference to matters pertaining to that branch of the business of the corporation is the knowledge of the corporation.[5] Facts coming to the knowledge of an agent while engaged about the business of his agency, are, in law,

[1] Thompson's Corps., § 3893; Dispatch Line v. Bellamy, etc., Co., 12 N. H. 205, 37 Am. Dec. 203; Delaware, etc., Co. v. Pennsylvania, etc., Co., 21 Pa. St. 131.

[2] Ohio, etc., R. Co. v. McPherson, 35 Mo. 13, 86 Am. Dec. 128.

[3] Wilson v. Kings, etc., R. Co., 114 N. Y. 487, 27 N. Y. St. Rep. 81. Appointment of an officer. Ellis v. North Carolina Inst., 68 N. C. 423.

[4] See Wilgus' Cases.

[5] Cragie v. Hadley, 99 N. Y. 131; Smith v. Board, etc., 38 Conn. 208; Atlantic, etc., Mills v. Indian, etc., Mill (Mass.), 17 N. E. Rep. 496; Loring v. Brodie, 134 Mass. 453; Johnson v. Shortridge (Mo., 1887), 6 S. W. Rep. 64; Huron, etc., Co. v. Kittleson (S. Dak.), 57 N. W. Rep. 233; Merchants Nat'l Bank v. Lovitt, 114 Mo. 519; Casco Nat'l Bank v. Clark, 139 N. Y. 307, 314; Johnson v. First Nat'l Bank, 79 Wis. 440, 24 Am. St. Rep. 722.

presumed to be known to the principal.[1] This applies to all agents of corporations of whatever degree as notice to an "agent of a corporation with respect to a matter covered by his agency must be as efficacious as to its directors or its president, since these are only agents, with larger powers and duties, it is true, but not more fully charged with respect to the particular thing than he whose authority is confined to that one thing."[2] Where the treasurer of a bank stole money from another person and placed it with the funds of the bank in order to cover a defalcation which was not known by the other officers, the bank acquired no title to the money as against the true owner, as it was charged with knowledge of the facts.[3] Notice to a director is not notice to the corporation except "in the business to which the knowledge is material through the agency of such director acting either alone or as one of the board."[4] The question always is, was the knowledge obtained while engaged in the business of the corporation?[5] The knowledge of an agent acquired in the course of the corporate business is notice to the corporation.[6] Knowledge, obtained by an agent of a corporation while engaged in

[1] Consolidated, etc., Co. v. Kansas, etc., Co., 45 Fed. Rep. 7; Slattery v. Schwannecke, 118 N. Y. 543.

[2] Saint v. Wheeler, etc., Co., 95 Ala. 362, 10 So. Rep. 539.

[3] Atlantic Cotton Mills v. Indian Orchard Mills, 147 Mass. 268; Huron, etc., Co. v. Kittleson, 4 S. Dak. 520, 57 N. W. Rep. 233.

[4] Buttrick v. Nashua, etc., R. Co., 62 N. H. 413; Nat'l Security Bank v. Cushman, 121 Mass. 490; Davis, etc., Co. v. Davis, etc., Co., 20 Fed. Rep. 699.

[5] Bank v. Clark, 139 N. Y. 307, 36 Am. St. Rep. 705. A corporation has knowledge of facts which are known to all its officers and stockholders. Holly Mfg. Co. v. New Chester, etc., Co., 48 Fed. Rep. 879. The knowledge of the principal promoter of a corporation, who acquired his knowledge as such, and who upon the organization of the corporation became its president and manager, is the knowledge of the corporation. Huron, etc., Co. v. Kittleson (S. Dak., 1894), 57 N. W. Rep. 233. Where the secretary and manager owned or controlled a large part of the capital stock, and managed the business as he pleased for the purpose of advancing his own interests, his knowledge was held to be the knowledge of the corporation. Anderson v. Kinley (Iowa, 1894), 58 N. W. Rep. 909. Where a corporation takes title to real estate through the incorporators, all of whom had knowledge of a defect in the title, it is charged with notice of such defect. Simmons, etc., Co. v. Doran, 142 U. S. 417.

[6] Willard v. Denise, 50 N. J. Eq. 482, 26 Atl. Rep. 29.

another transaction is not the knowledge of the corporation.[1] A corporation is not chargeable with the knowledge of one of its officers acquired in a matter in which the officer acts on his own behalf and in his own interest and does not represent the corporation.[2]

Where a defective deed purported to convey certain lands, one of the directors of a corporation, while not acting for the corporation, saw the record, but did not inform any of the agents of the corporation, and it was held that the corporation was not charged with knowledge of the facts.[3]

§ 535. **Compensation.**—Neither the directors nor other officers are entitled to compensation for ordinary official services unless it is provided for by the charter or by-laws adopted by the stockholders.[4] But if the director is employed to perform extraordinary services which do not pertain to his office of director, he is entitled to the reasonable or agreed value of such services.[5] Directors and other officers can not fix their own

[1] Fairfield, etc., Bank v. Chase, 72 Maine 226; Constant v. University, 111 N. Y. 604.

[2] Buffalo Co. Nat'l Bank v. Sharpe (Neb., 1894), 58 N. W. Rep. 734; Koehler v. Dodge, 31 Neb. 328; Barnes v. Gas, etc., Co., 27 N. J. Eq. 33; Bank v. Christopher, 40 N. J. Law 435; Wickersham v. Zinc Co., 18 Kan. 481; Merchants' Bank v. Lovitt, 114 Mo. 519; Farmers', etc., Bank v. Payne, 25 Conn. 444; Frenkel v. Hudson, 82 Ala. 158; Innerarity v. Bank, 139 Mass. 332; Casco Nat'l Bank v. Clark, 139 N. Y. 307.

[3] Farrell Foundry Co. v. Dart., 26 Conn. 376.

[4] Crumlish v. Central, etc., Co., 38 W. Va. 390, 23 L. R. A. 120; Martindale v. Wilson-Case Co., 134 Pa. St. 348, 19 Am. St. Rep. 706; American Central R. Co. v. Miles, 52 Ill. 174; Holder v. Railway Co., 71 Ill. 106; Jones v. Morrison, 31 Minn. 140; Citizens' Nat'l Bank v. Elliott, 55 Iowa 104, 39 Am. Rep. 167; Maux, etc., Co. v. Branegan, 40 Ind. 361; New York, etc., R. Co. v. Ketchum, 27 Conn. 170. See note in 16 Am. St. Rep. on compensation of directors. A vote of the directors of a corporation authorizing the president to draw one hundred dollars per month in addition to his salary to be used "for all special purposes" in connection with its business will not be assumed to be for an unlawful purpose. Clark v. American, etc., Co., 86 Iowa 436, 17 L. R. A. 557. See In re Anglo-Austrian, etc., Co., 61 L. J. Ch. 481, 7 Eng. Rul. Cas. 600, with English and American notes. See, also, Pew v. First Nat'l Bank, 130 Mass. 391, and Fitzgerald, etc., Co. v. Fitzgerald, 137 U. S. 98.

[5] Corinne, etc., Co. v. Joponce, 152 U. S. 405; Santa Clara, etc., Co. v. Meredith, 49 Md. 389, 33 Am. Rep. 264; Citizens Nat'l Bank v. Elliott, 55 Iowa 104, 39 Am. Rep. 167; Rogers v. Hast-

compensation. Unless otherwise provided by charter the directors may fix the compensation of other officers, but they have no authority to appropriate the funds in paying claims which the corporation is under no legal or moral obligation to pay, as for past services which have been rendered and paid for at a fixed salary previously agreed upon, or under a previous agreement that there should be no compensation.[1] An officer who is also a director can not vote on a proposition to fix his own salary.[2]

In a recent case in the United States Circuit Court of Appeals, Judge Sanborn said:[3] "Ordinarily the employment of a servant by a corporation raises the implication of a contract to pay fair wages or a reasonable salary for the services rendered, because it is the custom to pay such compensation and men rarely sacrifice their time and expend their labor or their money in the service of others without reward. Directors of corporations, however, usually serve without wages or salary. They are generally financially interested in the success of the corporation they represent, and their service as directors secures its reward in the benefit which it confers upon the stock which they own. In other words, the custom is to pay the ordinary employes of corporations for the services they render, but it is the custom of directors of corporations to serve gratuitously, without compensation or the expectation of it. The presumption of law follows the custom. From the employment of an ordinary servant, the law implies a contract to pay him. From the service of a director the implication is that he serves gratuitously. The latter presumption prevails, in the absence of an understanding or an agreement to the contrary, when directors are discharging the duties of other officers of the corporation to which they are chosen by the directory, such as those of president, secretary and treasurer. More-

ings, etc., R., 22 Minn. 25; Ten Eyck v. Pontiac, etc., R. Co., 74 Mich. 226; Illinois, etc., Co. v. Hough, 91 Ill. 63. A director may recover for services as superintendent. Harris v. Lemming, etc., Co. (Tenn.), 43 S. W. Rep. 869.

[1] Jones v. Morrison, 31 Minn. 140.

[2] Jones v. Morrison, 31 Minn. 140; Miner v. Ice Co., 93 Mich. 97.

[3] National, etc., Co. v. Rockland Co. (C. C. A.), 94 Fed. Rep. 335.

over, as the members of boards of directors act in a fiduciary capacity, they are without the power or authority to dispose of the property of the corporation without consideration. Consequently they may not lawfully vote back pay to an officer who has been serving a corporation voluntarily without any agreement that he shall receive any reward for the discharge of his duties. It is beyond their powers to create a debt of the corporation by their mere vote or resolution. * * * Some authorities have gone so far as to hold that officers of a corporation, who are also its directors, can not recover for the discharge of their duties unless their compensation is fixed by a by-law or a resolution of the board before their services are rendered.[1] The fact is, however, that in the active, and actual business transactions of the world, many officers of corporations, who are also members of their boards of directors, spend their time and their energies for years in the interest of their corporations, and greatly benefit the owner of the stock, under agreements that they shall have just, but indefinite, compensation for their services. We are unwilling to hold that such officers should be deprived of all compensation because the amounts of their salaries were not definitely fixed before they entered upon the discharge of their duties. A thoughtful and deliberate consideration of this entire question, and an extended consideration of the authorities upon it, has led to the conclusion that this is the true rule: Officers of a corporation who are also directors, and who without any agreement, express or implied, with the corporation or its owners, or their representatives, have voluntarily rendered their services, can recover no back pay or compensation therefor; and it is beyond the power of the board of directors, after such services are rendered, to pay for them out of the funds of the corporation, or to create a debt of the corporation on account of them.[2] But such officers

[1] Gridley v. Railroad Co., 71 Ill. 200; Kilpatrick v. Bridge Co., 49 Pa. St. 118-127; Wood v. Manufacturing Co., 23 Ore. 23.

[2] Jones v. Morrison, 31 Minn. 140; Blue v. Bank, 145 Ind. 518; Doe v. Transportation Co., 78 Fed. Rep. 62; Association v. Stonemetz, 29 Pa. St. 534; Railroad Co. v. Ketchum, 27 Conn. 170; Road Co. v. Branegan, 40 Ind. 361.

who have rendered their services under an agreement, either express or implied, with the corporation, its owners or representatives, that they shall receive reasonable but indefinite compensation therefor, may recover as much as their services are worth; and it is not beyond the power of the board of directors to fix and pay reasonable salaries to them after they have discharged the duties of their offices.''[1] It was therefore held that when, after the organization of the corporation, it was agreed and understood at an informal meeting of all the stockholders that the officers should be paid a reasonable compensation for their services, and by a by-law the board of directors was given power to fix the compensation of officers, their subsequent act in voting the president reasonable salary for past services was legal and that a note executed therefor by the corporation was binding on the corporation.

The officers may be compelled to account for all sums withdrawn for salaries where they have voted and paid the salaries largely for the purpose of depriving the stockholders of the results of a successful issue of pending litigation, although a part was paid for actual services rendered.[2]

§ 536. **Removal from office.**—There appears to be no well defined power to remove corporate officers from office. Officers and agents who do not hold under a contract for a fixed period may, of course, be removed without cause at any time. Those who hold for a definite time may be removed by the body which elected or appointed them for cause, or without cause, being liable for damages for breach of contract.[3] An officer who is elected to fill an office, the tenure of which is fixed by the charter, can not be removed until the expiration

[1] Missouri, etc., Co. v. Richards, 8 Kan. 101; Rogers v. Railway Co., 22 Minn. 25-27; Railroad Co. v. Tiernan (Kan.), 15 Pac. Rep. 544, Wilgus' Cases; Stewart v. Railroad Co., 41 Fed. Rep. 736; Rosborough v. Canal Co., 22 Cal. 556.

[2] Eaton v. Robinson, 19 R. I. 146, 29 L. R. A. 100.

[3] In re Griffing, etc., Co. (N. J.), 41 Atl. Rep. 931; Thomp. Corp., §§ 802, 805; Hunter v. Sun, etc., Co., 26 La. An. 13; Rex v. Richardson, 1 Burrow's Repts. 517, Wilgus' Cases. See also Imperial, etc., Hotel Co. v. Hampson, L. R. 23, Ch. Div. 1.

of the term. One who accepts a corporate office is bound by notice of a by-law which provides a method of removal from the office.[1] The right to an office can be determined only by a *quo warranto*.[2] Directors have no power to remove one of their number, or other officer elected by the stockholders, even for cause,[3] and the rule seems to be that even the shareholders have no inherent power to remove a director who has been elected for a definite time, as his election is a contract between him and the members of the company.[4] But where the removal of a director is absolutely necessary to the protection of a corporation a member may apply to a court of equity which will grant such relief as justice requires.[5]

§ 537. **Creditors can not control management.**[6]—The general rule that a simple contract creditor can not come into equity and have the property of his debtor subjected to the payment of his claim applies to corporations as well as to natural persons. Until he has secured a specific lien, the corporation may manage its property free from the control of its creditors, as there is no direct or express trust attached to the property. The mere fact of the existence of the relation of debtor and creditor gives the creditor no right to interfere with the management of the corporation by restraining it from the making of contracts and the disposing of its property. "The plaintiffs were simple contract creditors of the company. Their claims had not been reduced to judgment, and they had no express claim by mortgage, trust deed or otherwise. It is the settled law of this court that such creditors can not come into equity and obtain the seizure of the property of the debtor, and its application to the satisfaction

[1] Douglass v. Merchants', etc., Co., 118 N. Y. 484.

[2] Perry v. Oil Mill Co., 93 Ala. 364; Johnston v. Jones, 23 N. J. Eq. 216; Neall v. Hill, 16 Cal. 145, 76 Am. Dec. 508; People v. Albany, etc., R. Co., 5 Lans. 25.

[3] Nathan v. Tompkins, 82 Ala. 437; Commonwealth v. Detwiller, 131 Pa. St. 614, 7 L. R. A. 357.

[4] Imperial, etc., Co. v. Hampson, L. R. 23, Ch. Div. 1. See, generally, Burr v. McDonald, 3 Grat. (Va.) 215; State v. Bryce, 7 Ohio (Pt. 2) 82; Bayless v. Orn, Freem. Ch. 161–176.

[5] Morawetz Priv. Corp. 1, § 542. See State v. Vicker, 14 Am. St. Rep. 675.

[6] See Wilgus' Cases, Rights of Corporation as Against Creditors.

of their claims, and this, notwithstanding a statute of this state may authorize such a proceeding in the courts of the state. The line of demarcation between legal and equitable remedies in the federal courts can not be obliterated by state legislation. Nor is it otherwise in case the debtor is a corporation and an unpaid stock subscription is sought to be enforced."[1] Before a court of equity will take jurisdiction, the case must be brought under one of the recognized heads of equity jurisdiction, such as fraud or breach of trust. Where a creditor attempted to enjoin the making of a lease the court said:[2] "The plaintiffs can not maintain this bill unless upon the ground that any creditor can maintain a bill in equity against an individual debtor upon like allegations. But there is no allegation of fraud or breach of trust or any other ground of jurisdiction which brings the case within the general equity powers of a court of chancery. The bill is an attempt by a creditor to restrain his debtor from making what is alleged to be an improvident contract. The rights of the parties are governed by the rules of the common law. The plaintiffs, as creditors, might by an attachment have obtained security which would take precedence of the contemplated lease; but if they could not, the court has no power to restrain the debtor from making a disposition of his property which is permitted by the common law unless fraud or a breach of trust is alleged and shown. The allegation that the defendant corporation is insolvent does not aid the plaintiffs. In the absence of a statute giving the power, this court has no authority to act as a court of insolvency for the liquidation of the affairs of an insolvent railroad corporation."

Where the creditors of a corporation sought to enjoin it from issuing debenture stock and doing other *ultra vires* acts, Lord Hatherly said:[3] "The only remedy for a creditor in that case is to obtain his judgment and take out execution; or

[1] Hollins v. Brierfield, etc., Co., 150 U. S. 371; Tube Works v. Ballou, 146 U. S. 517; Cattle Co. v. Frank, 148 U. S. 603.

[2] Pond v. Framingham, etc., R. Co., 130 Mass. 194.

[3] Mills v. Railway Co., L. R. 5 Ch. App. 621.

it may be that he may have a power, if the case warrants it, of applying to wind up the company. But it is wholly unprecedented for a mere creditor to say, 'Certain transactions are taking place within the company, and dividends are being paid to shareholders which they are not entitled to receive, and, therefore, I am entitled to come here and examine the company's deed, to see whether or not they are doing what is *ultra vires*, and to interfere in order that, as by a bill *quia timet*, I may keep the assets in a proper state of security for the payment of my debt whensoever the time arrives for its payment.'" Sales and transfers of the corporate property can be questioned only by those creditors who have a specific lien, or have reduced their claims to judgment, and as judgment creditors assert that such transfers are fraudulent as to them.[1] Fraudulent conveyances and transfers of corporate property for the purpose of delaying creditors are governed by the same rules as similar conveyances by natural persons, and only those who became creditors prior to the transfer in question can complain.[2]

[1] Scott v. Neely, 140 U. S. 106.

[2] Graham v. Railway Co., 102 U. S. 148; Sutton, etc., Co. v. Hutchinson, 11 C. C. A. 320, 63 Fed. Rep. 496. As to the effect of a transfer to a new corporation, see Montgomery, etc., Co. v. Dienelt, 133 Pa. St. 585; Gray v. Steamship Co., 115 U. S. 116.

CHAPTER 19.

THE COMMON LAW LIABILITY OF STOCKHOLDERS.

§ 538. In general.
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540. Acts prior to incorporation.
541. The incorporation of a partnership business.
542. Debts contracted before distribution of stock.
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556. Decree determining assets and debts, and making assessments—Conclusiveness.
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§ 538. **In general.**—The liability of a stockholder at common law is determined and measured by the contract of subscription. When this contract with the corporation is fully performed, there is no further liability to the corporation or to its creditors. This freedom from personal liability was originally the distinctive feature of a corporation and was the principal inducement for the organization of business corporations rather than the formation of partnerships and joint stock companies. But within recent years many constitutions and legislatures have, upon grounds of supposed public policy, imposed additional liability upon stockholders for the benefit of creditors of corporations. Many statutes simply declare a liability which already existed at common law. The liability which results from a failure to become properly incorporated is not strictly an imposed liability but rather a liability for debts created when there were no stockholders and hence when the persons claiming to be such were not entitled to the protection afforded by the relation.

§ 539. **Liability to corporation measured by the contract of subscription.**—The common law liability of a stockholder to a corporation is simply a question of contract between him and the corporation, and, in the absence of a statutory or constitutional provision to the contrary, all liability is terminated by the payment of the full par value of his stock.[1] He is not, therefore, liable for the debts of the corporation unless made so by law or special contract.[2] The rule is exactly the reverse in the case of the members of a joint stock company who are liable jointly and severally for the debts of the company unless restricted by statute.[3] The members of a corporation may enlarge their liability over that imposed by the charter by contract, but not, by by-laws or resolutions without the consent of all those who are to be affected thereby.[4] The statutory liability may be contractual in its nature, as one who becomes a stockholder is charged with the knowledge of the laws which create the corporation and impliedly contracts with all who become creditors of the corporation that he will assume the liability imposed by the law.[5] But there is no privity between such a stockholder and the creditors of the corporation, and it is only after the insolvency of the corporation and in a proper equitable or statutory proceeding that the creditors have any right against such stockholder. The stockholder is, however, in all cases liable in some form of proceeding to pay according to the terms of his contract what remains unpaid on his subscription.[6] As a general rule, there is no liability to creditors after the corporation has become insolvent unless a liability to the corporation

[1] Gainey v. Gilson, 149 Ind. 58, 48 N. E. Rep. 633. It must be remembered, however, that the liability may be measured by the apparent rather than the actual contract between the subscriber and the corporation. See notes on liability of stockholders in 99 Am. Dec. 432, and 27 Am. L. Reg. (U. S.) 168. Liability of directors, see § 502, *supra*, Tradesmen's Pub. Co. v. Car Wheel Co., 95 Tenn. 634.

[2] Shaw v. Boylan, 16 Ind. 384; Coffin v. Rich, 45 Maine 507, 71 Am. Dec. 559.

[3] Walburn v. Ingilby, 1 Myl. & K. 61, 76; Frost v. Walker, 60 Maine 468.

[4] Trustees v. Flint, 13 Met. (Mass.) 539; Flint v. Pierce, 99 Mass. 68, 96 Am. Dec. 691.

[5] § 564, *infra*. Nimick v. Mingo, etc., Co., 25 W. Va. 184; Flash v. Conn, 109 U. S. 371.

[6] Walker v. Lewis, 49 Tex. 123; Warfield, etc., Co. v. Marshall, etc., Co., 72 Iowa 666, 2 Am. St. Rep. 263.

exists or the stockholder has by his conduct estopped himself from availing himself of his defense.[1] A release by the corporation is not always good as against the creditors of the corporation.[2] A bona fide purchaser of shares in the market, under the belief that they are paid up, is not liable to the creditors of the corporation, for the par value, although the representations of the corporation prove to be false.[3] The liability usually attaches to the person whose name appears as the owner of the stock upon the books of the corporation.[4] If there is no ground for estoppel, a person to whom shares of stock are issued by a corporation as security for a debt is not liable to the corporation or its creditors as a stockholder.[5]

§ 540. **Acts prior to incorporation.**—Personal liability may attach to parties for acts done before they become members, but while engaged in the organization of the corporation. Unless such contracts are expressly conditioned upon the incorporation of the company, and its ratification of their acts, the promoters are personally liable thereon.[6] The relation is similar to that of an agent of an undisclosed principal.[7] If the corporation after its creation ratifies the act of the promoter, the creditor may proceed against either.[8] The promoters are liable for such preliminary expenses as they have authorized, but they are not partners and there is no presumption of agency to act one for the other. It must be shown that the contract was made with the party or his authorized agent.

§ 541. **The incorporation of a partnership business.**—The liability of the members of a partnership on existing contracts is not affected by a change from a partnership to a corpora-

[1] Union, etc., Assn. v. Seligman, 92 Mo. 635, 1 Am. St. Rep. 776; Burgess v. Seligman, 107 U. S. 20; First Nat'l Bank v. Gustin, etc., Co., 42 Minn. 327, 18 Am. St. Rep. 510,

[2] See Upton v. Honsborough, 3 Biss. 417; Thompson's Corps., § 1517.

[3] Young v. Erie, etc., Co., 65 Mich. 111; Johnson v. Lullman, 15 Mo. App. 55, 88 Mo. 567.

[4] Crease v. Babcock, 10 Met. (Mass.) 525.

[5] § 569. Burgess v. Seligman, 107 U. S. 20; Fisher v. Seligman, 7 Mo. App. 383; Thompson's Corps., § 2935.

[6] *Ante*, § 55.

[7] Hurt v. Salisbury, 55 Mo. 310.

[8] Whitwell v. Warner, 20 Vt. 425; Kelner v. Baxter, L. R. 2 C. P. 174.

tion.[1] But if, as is often the case, the firm name is retained as the name of the corporation, it is incumbent upon the members to advertise the fact of the change,[2] and a failure to do so will render the members liable as partners to parties who become creditors after the incorporation without knowledge of the fact of incorporation.[3]

§ 542. **Debts contracted before distribution of stock.**—It seems that, in the absence of a statute, the members of a corporation are jointly and severally liable for debts contracted after the incorporation is completed, but before the capital stock is distributed.[4] Where the members are by statute made liable for the debts of the corporation contracted before the capital stock is paid in, and a certificate thereof recorded, the liability attaches to all who were stockholders when the debt was contracted, and are such when the liability is sought to be enforced, but not to those who became stockholders after the debt was contracted, and disposed of their shares before the action was brought.[5]

§ 543. **Liability resulting from illegal or defective incorporation.**[6]—There is much diversity of opinion as to the liability of the members of a defectively or irregularly organized corporation. It is generally conceded that persons who attempt to form a corporation will not escape individual liability if they do not so far comply with the law as to create at least a *de facto* corporation. In order to secure the exemption which results from incorporation it is, at the least, necessary that the corporation be of such a character as to be able to defend its right to exist as against all persons except the state.[7] An incorporation which is merely a cloak to cover illegal transactions will

[1] Broyles v. McCoy, 5 Sneed (Tenn.) 602.

[2] Martin v. Fewell, 79 Mo. 401, Wilgus' Cases.

[3] McGowan v. American, etc., Co., 121 U. S. 575; McFall v. McKeesport, etc., Co. (Pa.), 16 Atl. Rep. 478.

[4] Hawes v. Anglo-Saxon, etc., Co., 101 Mass. 385; First Nat'l Bank v. Almy, 117 Mass. 476. Compare Burnap v. Haskins, etc., Co., 127 Mass. 586.

[5] Sayles v. Bates, 15 R. I. 342.

[6] See Wilgus' Cases, particularly De Facto Corporations and Corporations by Estoppel.

[7] See Taylor Priv. Corp., § 148; Morawetz Priv. Corp., § 748.

not protect the stockholders from personal liability.[1] If the corporation is illegal or not even *de facto*, the members are generally held liable for the debts, either as partners, or on some principle of the law of agency. Where the public policy of the state forbids the organization of corporations for certain kinds of business, those who organize a corporation to carry on such business are liable as partners, and those who deal with them in the assumed corporate name are not estopped.[2]

§ 544. **Liability as partners.**—In order that there may be exemption from personal liability there must be either a legal incorporation, the existence of a *de facto* corporation, or of a condition of affairs which will raise an estoppel as against parties who might otherwise deny the fact of incorporation. In some cases it is held that where parties attempt to organize a corporation and fail to comply with the statutory provisions, requisite to legal incorporation, they are liable to creditors as partners.[3] It has also been held that the fact that a person has dealt with such an organization as a corporation will not estop him from repudiating a contract and holding the members of the defective organization as partners.[4] This, however, is manifestly inconsistent with the generally admitted rule that one who deals with a *de facto* corporation as such can not thereafter be heard to deny its legal existence. Where the liability exists it is only on the part of those who were members at the time the debt was contracted.[5] It exists only when the corporation is created for the purpose of carrying on a commercial business for the profit of its members. If the object of the organization is other than commercial although pecu-

[1] McGrew v. City Produce Exch., 85 Tenn. 572, 4 Am. St. Rep. 771; Paterson v. Arnold, 45 Pa. St. 410.

[2] Empire Mills v. Alston, etc., Co. (Tex. App.), 15 S. W. Rep. 505, 12 L. R. A. 366, annotated.

[3] Bigelow v. Gregory, 73 Ill. 197; Coleman v. Coleman, 78 Ind. 344; Martin v. Fewell, 79 Mo. 401, Wilgus' Cases; Richardson v. Pitts, 71 Mo. 128; Abbott v. Omaha, etc., Co., 4 Neb. 416; Whipple v. Parker, 29 Mich. 369; Garnett v. Richardson, 35 Ark. 144. In some states a liability as partners is imposed by statute. Heuer v. Carmichael, 82 Iowa 288; Abbott v. Omaha, etc., Co., 4 Neb. 416. See note on partnership liability of stockholders in case of defective or illegal incorporation, 17 L. R. A. 549.

[4] Empire Mills v. Alston Grocery Co., *supra*, and cases there cited.

[5] Fuller v. Rowe, 57 N. Y. 23; Stafford Bank v. Palmer, 47 Conn. 443.

niary profit may result to the members, they will not be liable for the debts of the corporation unless they have authorized or ratified the contracts.[1]

§ 545. **Conflicting theories and decisions.**—After noting the conflict among the decisions, and that in some states a liability as partners is imposed by statute, Judge Thompson says:[2] "Outside of the question of the existence of such statutes, and chiefly in jurisdictions where they do not exist, there is a class of cases holding to the simple, just and easily applied doctrine that where a number of coadventurers assume or attempt, under the provisions of a general statute, to organize themselves into a corporation, and fail to take the steps which that statute makes essential to their becoming incorporate, and assume to contract corporate debts without having taken such steps they are liable for such debts as partners.[3] Totally opposed to these conceptions is the doctrine of some of the courts that, in the case last named, the shareholders in the defectively organized corporation do not become liable as partners, general or special.[4] These cases, in general, proceed upon the theory that the members are not in such a case, liable as partners, (*a*) because they have not agreed among themselves to be so liable, (*b*) because they have not agreed with the other party to the contract to be so liable, (*c*) because they have not held themselves out to him as partners; and some of them fall back upon the well-known doctrine[5] that a partnership is not necessarily formed by an abortive agreement to form a corporation;[6] and some of them dwell upon the impropriety of the courts making contracts between parties which they have not made between themselves. Finally there is a class of cases maintaining the doctrine that where the corporation has been

[1] Bigelow v. Gregory, 73 Ill. 197; Johnson v. Corser, 34 Minn. 355.

[2] Thompson's Corps, § 2992.

[3] Bigelow v. Gregory, 73 Ill. 197; Coleman v. Coleman, 78 Ind. 344; Garnett v. Richarson, 35 Ark. 144; Abbott v. Omaha, etc., Co., 4 Neb. 416.

[4] Fay v. Noble, 7 Cush. (Mass.) 188, Wilgus' Cases; Trowbridge v. Scudder, 11 Cush. (Mass.) 83; First Nat'l Bank v. Almy, 117 Mass. 476; Stafford Nat'l Bank v. Palmer, 47 Conn. 443; Central City, etc., Bank v. Walker, 66 N.Y. 424; Blanchard v. Kaull, 44 Cal. 440, 450.

[5] See Thompson's Corps., § 421.

[6] Blanchard v. Kaul, 44 Cal. 440.

defectively organized, but nevertheless has a *colorable organization*, and exists and carries on its business as a corporation *de facto*, the state not electing to interfere,—there being no fraud nor any statute making the stockholders individually liable,—one who enters into a contract with it as a corporation estops himself from attempting to enforce the contract against its members as partners or original undertakers.[1] The general theory of these cases is that the creditor is estopped by his own contract from so proceeding against the stockholders, and that he will not be allowed in the face of his own contract to impeach the franchise of a *de facto* corporation, so long as the state is content that it should exist. It is conceded in some of the cases that this principle can have no application in a case where the corporation does not exist *de facto*, but is a mere pretense or usurpation; and in reason and justice it is absolutely essential to the support of this view that there should be a corporation having a corporate fund answerable for the debt as fully as though the organization of the corporation had been legally efficient."

§ 546. **The tendency of the decisions.**—The tendency of the decisions is toward holding that no partnership liability attaches where the parties acted in good faith and attempted to organize under a statute which authorized the organization of such a corporation. The weight of authority is in favor of protecting members from liability where business has been carried on in good faith, under the belief that the incorporation was valid.[2] To hold such persons as partners "involves not only the nullification of the contract which was actually contemplated by the parties, but the creation of a different contract, which neither of the parties intended to make."[3] Mr. Cook says: "During the past few years, however, the great

[1] Sniders, etc., Co. v. Troy, 91 Ala. 224, 11 L. R. A. Rep. 515, 24 Am. St. Rep. 887, Wilgus' Cases; Cory v. Lee, 93 Ala. 468; Planters' etc., Bank v. Padgett, 69 Ga. 159; American, etc., Co. v. Heidenheimer, 80 Tex. 344, 26 Am. St. Rep. 743.

[2] Rutherford v. Hill, 22 Ore. 218, 17 L. R. A. 549, annotated, Wilgus' Cases; Humphreys v. Mooney, 5 Colo. 282, and note. But mere intent to form a corporation is not enough. Martin v. Fewell, 79 Mo. 401, Wilgus' Cases.

[3] Morawetz Priv. Corp. 2, § 748; Planters' Bank v. Padgett, 69 Ga. 159.

weight of authority has clearly established the rule that when a supposed corporation is doing business as a *de facto* corporation, the stockholders can not be held liable as partners, although there have been irregularities, omissions or mistakes in incorporating or organizing the company. * * * It must be admitted that this conclusion of the law is reasonable and just. * * * The courts have gradually departed from the old decisions on this subject and have wisely refused to hold the stockholder liable. Recent cases have so settled the law beyond reasonable controversy.''[1]

Mr. Justice Brewer says:[2] ''I think the rule is this: that where persons knowingly and fraudulently assume a corporate existence, or pretend to have a corporate existence, they can be held liable as individuals; but where they are acting in good faith, and suppose that they are legally incorporated—that they are stockholders in a valid corporation—and where the corporation assumes to transact business for a series of years, and the assumed corporate existence is not challenged by the state, then they can not be held liable as individuals.'' In a recent Alabama case the court said:[3] ''The doctrine that a creditor who has dealt with a *de facto* corporation in its corporate capacity, can not charge the stockholders as partners with the corporate debts, there being no fraudulent intent alleged and proved, seems to us to be sustained by the weight of authority, maintained by stronger reasoning, consistent with well-settled principles, and in harmony with the policy of the state.''

[1] Cook Corps. 1, § 234; Whitney v. Wyman, 101 U. S. 392; Christian v. Bowman, 49 Minn. 99; Larned v. Beal (N. H.), 23 Atl. Rep. 149; Vanneman v. Young (N. J.), 20 Atl. Rep. 53; Bates v. Wilson (Colo.), 24 Pac. Rep. 99; Walton v. Riley, 85 Ky. 413; Welch v. Importers' Bank, 122 N. Y. 177; Reinhard v. Virginia, etc., Co. (Mo.), 18 S. W. Rep. 17; Seacord v. Pendleton, 55 Hun 579; Bushnell v. Consolidated, etc., Co. (Ill., 1891), 27 N. E. Rep. 596; Cory v. Lee, 93 Ala. 468; American, etc., Co. v. Heidenheimer, 80 Tex. 344. See, also, Finnegan v. Noerenberg, 52 Minn. 239, Wilgus' Cases.

[2] Gartside, etc., Co. v. Maxwell, 22 Fed. Rep. 197.

[3] Snider's Sons Co. v. Troy, 91 Ala. 224, 24 Am. St. Rep. 887, 11 L. R. A. 515, Wilgus' Cases.

§ 547. **Where there is not even a de facto corporation.**[1]— There is substantial agreement among the courts that where there is not even a *de facto* corporation, the associates are liable, either as partners or as agents, for obligations incurred in the name of the association. Thus, if there is no law authorizing the creation of such a corporation, or if the incorporating act is unconstitutional, all organizations effected thereunder will be treated as partnerships.[2] The liability of the

[1] See Wilgus' Cases, Corporations by Estoppel.

[2] Eaton v. United States, etc., Co., 76 Mich. 579, 6 L.R.A. 102; Johnson v. Corser, 34 Minn. 355; Guckert v. Hacke, 159 Pa. St. 303, Wilgus' Cases; Empire Mills v. Alston, etc., Co. (Tex.), 15 S. W. Rep. 200; Kaiser v. Bank, 56 Iowa 104; Bigelow v. Gregory, 73 Ill. 197; Abbott v. Refining Co., 4 Neb. 416; Coleman v. Coleman, 78 Ind. 344; Wechselberg v. Bank, 64 Fed. Rep. 90, 12 C. C. A. 56, Wilgus' Cases; Booth v. Wonderly, 36 N. J. L. 250; Vredenberg v. Behan, 33 La. Ann. 627. Sheren v. Mendenhall, 23 Minn. 92, was an action against Mendenhall and Baldwin as partners, under the name of the "State Savings Association." It appeared that the defendants undertook to become a corporation under the general laws, but the court held that the law under which it attempted to incorporate did not authorize the formation of such a corporation, and the defendants were held liable as partners. Johnson v. Corser, 34 Minn. 355, was a case not of irregularity in omitting to conform to some requirement of the law, but an attempt to organize a corporation such as was not authorized by the law. In an action against the members, all the parties concerned in or authorizing the contract personally were held liable, but the court refused to apply the doctrine of implied agency recognized in the law of partnership. The court said: "The plaintiff asserts, as a rule of law applicable to the case, that from the mere failure to perfect the contemplated incorporation, the association, after proceeding to carry on the proposed enterprise, became a partnership, and the members copartners, with authority, implied from the relation, in each member to bind all the associates by any act within the scope of the business carried on by the association. We can not sanction the application to this case of the doctrine of implied agency, as it is recognized in ordinary business copartnerships. * * * As far as appears, the business undertaken and carried on by the defendants, was not of a partnership character, nor the purpose such as to suggest the relation of co-partners between those engaged in it." In Foster v. Moulton, 35 Minn. 458, Wilgus' Cases, the court said: "It was manifest that the understanding between the members and the basis upon which the certificates of membership were issued, was a corporation in fact as it was in form. It is, at least as between the members themselves, to be treated as a corporation *de facto*, and the plaintiff estopped from treating the members as partners." See Finnegan v. Noernberg, 52 Minn. 239, Wilgus' Cases; Christian v. Bowman, 49 Minn. 99.

contracting parties is sometimes based upon the rule that by assuming to act for a principal that does not exist, the agent becomes personally liable, as for a breach of implied warranty to make good the undertaking.[1] Where an action was brought against a stockholder on a note given by a pretended corporation the court said:[2] "The apparent corporation was not a corporation. The statute of New Hampshire requires five associates, and the articles of agreement must be recorded in the town in which the principal business is to be carried on, and the place in which the business is to be carried on must be distinctly stated in the articles; otherwise there is no corporation. The defendant's pretended associates were associates only in name; he alone was interested in the enterprise. The articles of agreement were recorded in Nashua, and stated that the business was to be carried on there; but it was not in fact carried on there, and was not intended to be. The defendant took all the shares of the capital stock, and paid in, to himself, as treasurer, only fifty per cent. of the amount thereof. This is not a case where there has been a defective organization of a corporation which has a legal existence under a valid charter. Here there was no corporation. It was just the same as if the defendant had done nothing at all in the way of establishing a corporation, but had conducted his business under the name of the Forbes Woolen Mills, calling it a corporation. The business was his personal business, which he transacted under that name."

§ 548. **"One man" corporations.**[3]—The courts have had considerable trouble with what have come to be known as one man corporations. By the weight of authority the fact that all the shares of the stock have come into the hands of one person does not operate as a dissolution of the corporation, or make it a fraud upon the public for him to continue the busi-

[1] Thompson Corps., § 418.

[2] Montgomery v. Forbes, 148 Mass. 249, Wilgus' Cases.

[3] See Louisville Banking Co. v. Eisenman, 94 Ky. 83, 42 Am. St. R. 335, 19 L. R. A. 604, Wilgus' Cases.

ness in the corporate name.[1] In a celebrated English case it appeared that one Salomon was carrying on business as a merchant, and while solvent he organized a corporation for the purpose of taking over and carrying on his business. The memorandum of association was signed by Salomon, his wife, daughter and four sons, who each subscribed for one share. Twenty thousand shares were allotted to Salomon, who also received debentures amounting to ten thousand pounds, which constituted a first lien upon the property of the corporation. Subsequently these debentures were canceled, and others for the same amount at the request of Salomon issued to one Broderip as security for a loan of five thousand pounds, which was made to Salomon and by him loaned to the corporation. Broderip commenced an action to enforce his security. A receiver was appointed and an order for compulsory winding up made. The corporation owed unsecured debts to a large amount, of which more than one-half was owed to Salomon. The receiver paid Broderip's debt, and Salomon claimed the balance as the owner of the debentures. The receiver disputed the validity of the debentures on the ground of fraud, and claimed a rescission of the agreement for the transfer of the business, and the cancellation of the debentures. The trial court held that the company was a mere nominee of Salomon, and that the case stood as if the nominee instead of being a company had been merely some individual agent of Salomon, to whom he had proposed to sell his business. The trustee in bankruptcy would then have had the right to make Salomon indemnify the agent against the debts that he had contracted by the direction of his principal. The right of the liquidator was held to be precisely the same, notwithstanding the debentures (which were a mere form), intended to give the appearance of reality to a sale which was in fact no sale, because it was a sale by a man to an agent for his own profit. Salomon was required to indemnify the company against the

[1] Louisville, etc., Co. v. Kaufmann (Ky.), 48 S. W. Rep. 434. A sole stockholder who wrongfully caused all the property of the corporation to be transferred to him, may be held responsible for its debts. Angle v. Chicago, etc., R. Co., 151 U. S. 1.

amount of its unsecured debts, and a judgment was entered against him. Upon appeal the judgment was affirmed.[1]

Lord Justice Lindley said: "There can be no doubt that in this case an attempt has been made to use the machinery of the company's act for a purpose for which it never was intended. The legislature contemplated the encouragement of trade by enabling a comparatively small number of persons, namely not less than seven, to carry on business with a limited joint stock or capital and without the risk of liability beyond the loss of such joint stock or capital. But the legislature never contemplated an extension of limited liability to sole traders or to a fewer number than seven. In truth the legislature clearly intended to prevent anything of the kind for section 48 takes away the privilege conferred by the act from those members of limited companies who allow such companies to carry on business with less than seven members; and by section 79 the reduction of the number of members below seven is a ground for winding up of the company. Although in the present case there were and are seven members, yet it is manifest that six of them are members simply in order to enable the seventh himself to carry on business with limited liability. The object of the whole arrangement is to do the very thing which the legislature intended not to be done; and ingenious as the scheme is, it can not have the effect desired so long as the law remains unaltered. * * * The incorporation of the company can not be disputed. Whether by any proceeding in the nature of a *scire facias* the court could set aside the certificate of incorporation is a question which has never been considered, and on which I express no opinion; but be that as it may, in such an action as this the validity of the certificate can not be impeached. The company must, therefore, be regarded as a corporation, but as a corporation created for an illegitimate purpose." Lord Justice Lopes said: "The incorporation of the company was perfect. The machinery by which it was formed was in every respect perfect, every detail had been observed, but notwithstanding the business was in truth and fact the business of Aaron Salomon; he had the beneficial in-

[1] Broderip v. Salomon, L. R. (1895) 2 Ch. Div. 323.

terest in it; the company was a mere *nominis umbra*, under cover of which he carried on his business as before, securing himself against loss by a limited liability of one pound per share, all of which shares he practically possessed and obtaining a priority over the unsecured creditors of the company by the debentures, of which he had constituted himself the holder." Notwithstanding the fact that the incorporators had complied in every respect with the statute authorizing the organization of such companies the decision of the lower court was affirmed and the appeal of Salomon dismissed.

§ 549. **One-man corporations, continued.**—An entirely different view of the case was taken in the house of lords, where the order appealed from by Salomon was reversed,[1] where it was said that the only question of importance was whether the respondent company was a corporation, and in order to determine that question it was simply necessary to examine the statute. The lord chancellor said: "I must pause here to point out that the statute enacts nothing as to the extent or degree of interest which may be held by each of the seven, or as to the proportion of interest or influence possessed by one or the majority of the shareholders over the others. One share is enough. Still less is it possible to contend that the motive of becoming shareholders or of making them shareholders is a field of inquiry which the statute itself recognizes as legitimate. If they are shareholders, they are shareholders for all purposes, and even if the statute was silent as to the recognition of trusts I should be prepared to hold that if six of them were the *cestui que trusts* of the seventh, whatever might be their rights *inter se*, the statute would have made them shareholders to all intents and purposes with their respective rights and liabilities; and dealing with them in their relation to the company, the only relation which I believe the law would sanction, would be that they were corporators of a corporate body. * * * Either the limited com-

[1] Salomon v. Salomon, etc., Co., Lim., L. R. App. Cas. 1897, 22; 75 Law Times N. S. 427. See, also, Montgomery v. Forbes, 148 Mass. 249, Wilgus' Cases.

pany was a legal entity or it was not. If it was, the business belonged to it and not to Mr. Salomon; if it was not, there was no person and no thing to be an agent at all; and it is impossible to say at the same time that there is a company and there is not. * * * The truth is that the learned judges have never allowed in their own minds the proposition that the company has a real existence. They have been struck by what they considered the inexpediency of permitting one man to be, in influence and authority, the whole company, and assuming that such a thing could not have been intended by the legislature, they have sought various grounds upon which they might insert into the act some prohibition of such a result. Whether such a result be right or wrong, politic or impolitic, I say, with the utmost deference to the learned judges, that we have nothing to do with that question if this company has been duly constituted by law, and whatever may be the motives of those who constituted it, I must decline to insert into that act of parliament limitations which are not to be found there."

§ 550. **Corporations organized to do business exclusively in another state.**—The decisions are not uniform on the question as to whether a corporation can be created by one state with power to do business only in a state other than that of its creation. In Massachusetts and Texas such an incorporation will not protect the members from liability as partners.[1] The same doctrine was established in New Jersey[2] at an early day. This is the general rule where there is lack of good faith on the part of either the state or the corporators, as "no rule of comity will allow one state to spawn corporations, and send them forth into other states to be nurtured and do business there, when said first mentioned state will not allow them to do business within its own borders."[3] In New York and at present in New Jersey

[1] Montgomery v. Forbes, 148 Mass. 249, 19 N. E. Rep. 342, Wilgus' Cases; Empire Mills v. Alston (Tex. App.), 15 S. W. Rep. 200, 12 L. R. A. 366, annotated.

[2] In Hill v. Beach, 12 N. J. Eq. 31, the court said: "It is perfectly manifest on the face of their proceedings that their attempted organization, under the general laws of New York respecting corporations, was a fraud upon the law of this state."

[3] Land Grant, etc., Co. v. Coffey Co., 6 Kan. 245.

the stockholders will not be held liable as partners, although the corporation was created for the purpose of doing all its business in foreign states if there was no fraud or evasion of the laws of the state of incorporation.[1] In a recent case the court of appeals of New York said:[2] "Whatever inferences can be drawn as to the motives which took them into a foreign jurisdiction to organize a corporation under its laws, I agree with the general term that any such question has been once and for all settled by our recent decision in the case of Demarest v. Flack.[3] It appeared in that case that citizens of this state, incorporated under the laws of West Virginia, to carry on a certain business, with the principal office of the company in New York City, where only it had been conducting its operations. It was claimed that these facts invalidated the corporation, and that there was a manifest evasion of, and fraud upon, the laws of the state. But it was held that they constituted no

[1] Demarest v. Flack, 128 N. Y. 205, 13 L. R. A. 854; Merrick v. Van Santvoord, 34 N. Y. 208; Second Nat'l Bank v. Hall, 35 Ohio St. 158. See Wright v. Lee, 2 S. Dak. 596, 51 N. W. Rep. 706; Oakdale, etc., Co., v. Garst, 18 R. I. 484, 28 Atl. Rep. 973; Missouri, etc., Co. v. Reinhard, 114 Mo. 218; Trowbridge v. Scudder, 11 Cush. (Mass.) 83.

[2] Lancaster v. Amsterdam, etc., Co., 140 N. Y. 576, 35 N. E. Rep. 964.

[3] 128 N. Y. 205. In People v. Board of Assessors (N. Y.), N. Y. Law Journal of May 3, 1899, it was held by a divided court that the good will of a corporation organized under the laws of West Virginia by residents of New York for the purpose of doing business wholly in New York was capital employed in New York and therefore taxable in New York. The court said: "If we hold that the good will of a foreign corporation is not taxable here simply because it is intangible, although it grew up here, has a market value here and nowhere else, we place a premium on non-resident corporations by relieving them of a burden which we place upon domestic corporations. As was said in Martine v. International, etc., Soc., 53 N. Y. 339, 347: 'It would be most unreasonable for these foreign corporations to ask the privilege of doing business under our laws in competition with domestic institutions, and then ask exemption from the obligations and liabilities which attach to the latter.' It is a matter of common knowledge as well as of grave public concern in this state, that for the sake of a paltry license tax, certain sister states are competing with each other in granting loose charters without adequate protection for the public, and thus inducing the promoters of corporations to organize under their statutes, when there is no intention of investing capital or doing business in the state where the organization is affected. Such selfish and unfriendly legislation should not be encouraged by the court of the state which is most injured by it."

reason for refusing recognition to the corporation; that there was no essential difference between a corporation, formed under the laws of a foreign state, the members of which were its own citizens, and one so formed, the members of which were citizens of our own state. If our citizens are attracted to other jurisdictions for purposes of incorporation, because of more favorable corporation or taxation laws, I can not see in that fact, however, and in whatever sense to be deplored, any reason that they should be prevented from employing here the corporate capital in the various channels of trade or manufacture. That, as it seems to me, would be a rather hurtful policy, and one not to be attributed to the state."

§ 551. **Liability for capital wrongfully distributed.**—It has been held that if any portion of the capital is paid to the stockholders under the name of dividends it may be recovered by the representative of the creditor, although the stockholder had no knowledge but that the dividends had been earned and were properly paid. Equity will require such stockholders to contribute pro rata for the payment of the debts.[1] "The stockholders have no rights to anything but the residuum of the capital stock, after the payment of all the debts of the corporation. If before all such debts are discharged, they take into their hands any of the funds of the corporation, they hold them subject to an equity which it is against conscience to resist."[2] But the supreme court of the United States in a late case held that the receiver of a national bank can not recover a dividend paid entirely out of capital when the stockholder receiving the dividend acted in good faith, believing the same to be paid out of profits, and the bank at the time of the payment was not insolvent.[3] Legitimate profits form no part of the capital stock, and a stockholder can not be required to surrender bona fide dividends declared and distributed at a time when the corporation was solvent.[4]

[1] Minnesota, etc., Co. v. Langdon, 44 Minn. 37.

[2] Kohl v. Lilienthal, 81 Cal. 378; Clapp v. Peterson, 101 Ill. 26; Crandall v. Lincoln, 52 Conn. 73; Bartlett v. Drew, 57 N. Y. 587; Gratz v. Redd, 4 B. Mon. (Ky.) 178.

[3] McDonald v. Williams, 174 U. S. 397.

[4] Reid v. Eatonton, etc., Co., 40 Ga. 98, 2 Am. Rep. 563.

§ 552. **Liability upon shares issued below par.**—The rule that holds original subscribers to the stock of a corporation liable to pay the full face value of shares for the benefit of the creditors of the corporation, notwithstanding a contract with the corporation by which it has agreed to accept a less amount in full payment, has been already discussed.[1] Such a contract is valid as against the corporation, at least by estoppel,[2] but it is impeachable by parties who extend credit to the corporation after the issue of such stock.[3] The trust-fund theory, as originally established, required that the par value of the share must be paid into the corporation treasury when necessary to liquidate the claims of creditors, unless the stockholders are able to show a greater equity than that possessed by the creditors. But it has been considerably modified. "There is not much room to doubt the soundness of the conclusion that where the rights of creditors are not concerned, an agreement between the corporation and its shareholders that they are to have their shares upon the payment of a sum less than the par or nominal value will estop the corporation from maintaining an action to collect the balance. But it was formerly supposed, in conformity with the holding of the supreme court of the United States, just referred to, that a subscriber to the shares of a corporation could be compelled to pay, if necessary to liquidate its debts, the entire par value of his shares, no matter what agreement he may have made with the corporation in respect to their payment, at the time of his subscription or afterwards. But this doctrine, as already seen, has been recently modified by the supreme court of the United States, to the extent of holding that, in the absence of circumstances creating an *equitable estoppel* in favor of the creditor of the corporation, and against the shareholder, the latter can not be compelled to pay, even for the purpose of liquidating

[1] See § 329, *supra*. When shares are issued as full paid for property received in payment, there must be *actual fraud* in the transaction to enable the creditors of the corporations to hold the stockholder to a further liability. Fort Madison Bank v. Alden, 129 U. S. 372. See § 340, *supra*.

[2] *Ante*, § 329. Kenton, etc., Co. v. McAlpin, 5 Fed. Rep. 737.

[3] Washburn v. Green, 133 U. S. 30; Upton v. Tribilcock, 91 U. S. 45; Scovill v. Thayer, 105 U. S. 143.

the debts of the corporation after its insolvency, anything beyond what the corporation agreed with him to accept as full payment. This is tantamount to holding that, as far as the rights of creditors, who became such prior to the issuing of the shares, are concerned, whatever the corporation agreed to accept as payment is payment, even though it agreed to give away the shares, or to issue them as a bonus, or in consideration of some past benefit, it is to be deemed payment. This lifts the obligation of the shareholder to pay the par value of his shares, even for the purpose of liquidating the debts of the corporation, out of the category of principles of public policy, and lets it down to the mere doctrine of an equitable estoppel. The meaning is that, except in cases where creditors have been deceived and misled by the corporation pretending to have a capital which it has not, a creditor can enforce no right against a shareholder greater than the corporation itself could enforce against him."[1] This is believed to be an accurate statement of the law at the present time.

§ 553. **Fraudulent acts.**—The stockholders are not liable for the torts of the corporation, but they are liable for their own torts committed under pretense of acting for the corporation. Thus they "may have originally contracted debts in the name and upon the credit of the corporation, without any purpose of payment or without any reasonable probability that payment could be made by the corporation; or they may have diverted all the funds of the corporation to their own use, in either case evincing a settled purpose of defrauding creditors."[2] It was held that a stockholding creditor did not become personally liable for the corporate debts by securing a preference out of the corporate property. But in order to make the stockholders personally liable the creditor must show that he was induced to become such by their deceit.[3]

§ 554. **Enforcement—Defenses.**—A debt growing out of a contract of subscription may be enforced by the corpora-

[1] Thompson Corps., § 2953.

[2] Whitwell v. Warner, 20 Vt. 425; Medill v. Collier, 16 Ohio St. 599. See Swan Land, etc., Co. v. Frank, 148 U. S. 603.

[3] Sisson v. Matthews, 20 Ga. 848.

tion in an action at law, or after its insolvency by its assignee or receiver in an appropriate action for the benefit of its creditors.[1] Ordinarily the same defenses are available against the assignee or receiver as would have been available against the corporation. But the party may have put himself in such a position as to be unable to assert his defense against the creditors. Certain contracts, valid as between a subscriber and a corporation, are not, however, binding upon creditors of the corporation. Thus a contract between a corporation and a subscriber that the subscription is not to be collected or is to be payable only in part is void as against creditors of the corporation, although binding upon the corporation and the stockholders who assented to it.[2] A conditional subscription may be binding in favor of creditors, although the conditions have not been performed, if the subscriber has waived the condition by acting as a stockholder.[3] So certain conditions will be treated as void in favor of creditors. Thus, in some jurisdictions, a subscription made prior to incorporation is unauthorized and void, and will be treated as unconditional and binding.[4] A stockholder can not set up the illegality of the scheme of the corporation which did not appear on the face of the contract of subscription or the prospectus referred to in the contract in order to escape from liability to creditors whose debts have been contracted upon the faith of the subscription.[5] The liability for unpaid subscriptions, when imposed by the constitution of the state, can not be avoided by a provision in the charter which attempts to exempt the stockholders from such liability.[6]

[1] Hatch v. Dana, 101 U. S. 205. As to right of the creditor by bill in equity, or other appropriate proceedings, to have unpaid subscription subjected to the payment of his debt, see Hawkins v. Glenn, 131 U. S. 319; Handley v. Stutz, 139 U. S. 417.

[2] Burke v. Smith, 16 Wallace U. S. 390; Upton v. Triblicock, 91 U. S. 45.

[3] Cornell & Michler's Appeal, 114 Pa. St. 153.

[4] Burke v. Smith, 16 Wallace U. S. 390; Caley v. Railroad Co., 80 Pa. St. 363.

[5] Cardwell v. Kelly, 95 Va. 570, 40 L. R. A. 240.

[6] Van Pelt v. Gardner, 54 Neb. 701, 75 N. W. Rep. 874.

§ 555. **Enforcement of liability in a foreign jurisdiction.**[1]— The liability of a non-resident stockholder on his contract of subscription can be enforced in any forum where jurisdiction of the person can be obtained. The enforcement of this simple contract liability growing out of the express or implied promise to pay contained in the contract of subscription, is to be distinguished from the right to enforce the statutory liability which is considered elsewhere. The contract of subscription is governed by the laws of the state by which the corporation was created.[2] The right to recover unpaid subscriptions in another state should not be treated as resting upon the doctrine of comity, but upon the universally recognized right to enforce a valid contract wherever the defendant can be found.[3] The right to sue the stockholder in a foreign state rests upon his contract to pay for the shares, and, hence, it can not be maintained in those states which do not recognize an implied contract to pay as arising out of a mere subscription for shares.[4] A suit on an assessment against a stockholder, made under a decree of a court of the state, is enforcible in a foreign jurisdiction.[5] In some states the receiver of a foreign corporation is allowed to recover the amount of an unpaid subscription,[6] while in other states the right of a receiver to sue in a foreign jurisdiction is denied.[7] A creditor seeking to enforce the liability of a stockholder for an unpaid

[1] See Wilgus' Cases.

[2] Jessup v. Carnegie, 80 N. Y. 441, 36 Am. Rep. 643; Penobscot, etc., R. Co. v. Bartlett, 12 Gray 244, 71 Am. Dec. 753; Hancock Nat'l Bank v. Ellis, 166 Mass. 414, 42 L. R. A. 396; Bell v. Farwell, 176 Ill. 489. See also Stebbins v. Scott, 172 Mass. 356, 52 N. E. Rep. 535; Colling v. Dodge, 167 Mass. 231; Marshall v. Sherman, 148 N. Y. 9.

[3] Mandel v. Swan, etc., Co., 154 Ill. 177, 27 L. R. A. 313.

[4] New Haven, etc., Co. v. Linden, etc., Co., 142 Mass. 349.

[5] Morris v. Glenn, 87 Ala. 628. By an ancillary receiver. Baldwin v. Hosmer, 101 Mich. 119, 25 L. R. A. 739; Mutual, etc., Co. v. Phœnix, etc., Co. (Mich.), 34 L. R. A. 694; Western Nat'l Bank v. Lawrence (Mich.), 76 N. W. Rep. 105.

[6] Cuykendall v. Miles, 10 Fed. Rep. 342; Dayton v. Borst, 31 N. Y. 435; Mann v. Cooke, 20 Conn. 178; Pugh v. Hurtt, 52 How. Pr. 22; Baldwin v. Hosmer, 101 Mich. 119; Fawcett v. Sup. Sitting of I. H. (Conn.), 24 L. R. A. 815; Buswell v. Sup. Sitting, etc., 161 Mass. 224, 23 L. R. A. 846.

[7] Wyman v. Eaton (Ia.), 43 L. R. A. 695; Booth v. Clark, 17 How. (U. S.) 322; Beach on Receivers, § 683.

subscription should proceed by a creditor's bill,[1] although there are cases which hold that even after judgment against a corporation, the creditors must seek their remedy in the state where the corporation was created and there have the relations of the creditors and stockholders toward each other determined.[2]

§ 556. **Decree determining assets and debts, and making assessments—Conclusiveness.**[3]—It is now well settled that an assessment for an unpaid stock subscription made under a decree of a court of the corporate domicile is binding upon all the stockholders without reference to their residence or the fact of service. Some cases have held such a decree equivalent to a judgment against the individual stockholder, but these decisions have been modified by a recent decision of the supreme court of the United States. An order authorizing an assessment upon the capital of a state bank, made by a court under statutory authority upon the petition of the receiver, is binding upon all stockholders and can not be collaterally attacked by them, although they were non-residents and not before the court.[4] So an order and decree of the court of the corporate domicile appointing a receiver for an insolvent bank, ascertaining the deficiency and directing an assessment upon the stockholders, was held binding upon the stockholders who were not parties to the proceeding.[5] In proceedings in a court of another state to wind up a domestic corporation as an insolvent, in which the court has jurisdiction of the subject-mat-

[1] Lemcke v. Tredway, 45 Mo. App. 507, 94 Mo. 410. But judgment must first be obtained against the corporation in the state of the corporate domicile unless it is shown to be impossible. Rule v. Omega, etc., Co. (Minn.), 67 N. W. Rep. 60. And see Remington, etc., v. Samara Bay Co., 140 Mass. 494. § 576, *infra*.

[2] See § 579, *infra*. Young v. Farwell, 139 Ill. 326. In Turner Bros. v. Alabama, etc., Co., 25 Ill. App. 144, it was held that the creditor might proceed by way of attachment or garnishment.

[3] See Wilgus' Cases.

[4] Sheafe v. Larimer, 79 Fed. Rep. 921. As to the binding force of assessments by the court upon stockholders in insolvent corporations, wherein the court is the successor of the corporation, see Marson v. Deither, 49 Minn. 423; In re Minnehaha, etc., Assn., 53 Minn. 423; Hale v. Hardon, 95 Fed. Rep. 747. Call invalid for indefiniteness, North, etc., Co. (Wis.), 46 L. R. A. 174.

[5] Howarth v. Ellwanger, 86 Fed. Rep. 54; Hawkins v. Glenn, 131 U. S. 319. See Hale v. Hardon, 95 Fed. Rep. 747.

ter and of the corporation, the members thereof are parties through representation by the corporation and until attacked and set aside in appropriate judicial proceedings, an assessment made in the action upon the members is conclusive evidence in the courts of another state of the necessity for making the assessment and to that extent binds each of the members without notice to him.[1] Such a decree as to the amount of assets and debts of an insolvent mutual insurance company and of the amount of assessments necessary to liquidate its debts was held conclusive on a stockholder when sued in the courts of another state upon a note which was in the possession of the company and under the control of the court when the decree was made.[2]

§ 557. **Conclusiveness of decree, continued.**—The supreme court of the United States has modified its earlier decisions and now holds that, although such a judgment is conclusive so far as it establishes the amount of debts and liabilities of the corporation and the necessity for an assessment,[3] the stockholder may still plead any defense which goes to show that he is not liable on his contract of subscription, such as payment or the statute of limitations.[4] Mr. Justice

[1] Longworthy v. Garding (Minn.), 77 N. W. Rep. 207. Citing Telegraph Co. v. Purdy, 162 U. S. 329.

[2] Mutual, etc., Co. v. Phoenix, etc., Co., 108 Mich. 170, 34 L. R. A. 694, annotated. In Parker v. Lamb, 99 Iowa 265, 34 L. R. A. 704, it was held that one assessment on premium notes made by a receiver of a mutual insurance company under a decree of court is not an adjudication binding on the courts of another state as against a maker of one of such notes who was not a party to the proceedings which resulted in the assessment, and who before the bankruptcy of the company had surrendered his policy and received back his note.

[3] See Glenn v. Liggett, 135 U. S. 533; Hawkins v. Glenn, 131 U. S. 319; Glenn v. Springs, 26 Fed. Rep. 494; Lehman, etc., Co. v. Glenn, 87 Ala. 618; Glenn v. Williams, 60 Md. 93; Howard v. Glenn, 85 Ga. 238.

[4] Great Western, etc., Co. v. Purdy, 162 U. S. 329. In Warner v. Delbridge, etc., Co., 110 Mich. 590, 34 L. R. A. 701, the court said: "If this contract is to be treated as a Michigan contract the holding should be sustained, unless it be held that the order making the assessment, made at the *situs* of the home company, is conclusive, not only as to the authority to make the assessment, but as to the extent of the defendant's liability. This question was recently before the court in the case of Mutual, etc., Co. v. Phœnix, etc., Co., 108 Mich. 170, 34 L. R. A. 694, and the conclusion was then reached that the decision of a sister state is binding upon the courts of this state in all these re-

Gray said: "The order of that court was, in effect, as it was in terms, simply a call or assessment upon all stockholders who had not paid for their shares in full. It was such as the directors might have made before the appointment of a receiver; and in making it, the court, having by that appointment assumed the charge of the assets and affairs of the corporation, took the place and exercised the office of the directors.[1] The order of assessment, whether made by the directors as provided in the contract of subscription or by the court as the successor in this respect of the directors, was doubtless, unless directly attacked and set aside by appropriate judicial proceedings, conclusive evidence *of the necessity for making such an assessment* and to that extent bound every stockholder without personal notice to him.[2] But the order was not and did not pur-

spects. This conclusion was based upon the constitutional provision that full faith and credit shall be given in each state to the public acts, records and judicial proceedings of every other state. Art. 4, § 1. An examination of the decisions of the federal supreme court led us to the conclusion that a stockholder of a corporation is so far an integral part of the corporation that, in view of the law, he is privy to the proceedings touching the body of which he is a member, and that a determination that an assessment upon the policy-holders in a certain amount and for certain obligations of the company should be made was final and conclusive, and could not be attacked collaterally when suit was brought upon such assessment in a foreign state. In reaching this conclusion, the question involved being a federal question, we felt ourselves bound by the determination of the federal court in Hawkins v. Glenn, 131 U. S. 319, and Glenn v. Liggett, 135 U. S. 533. But since the decision of this court in Mutual, etc., Co. v. Phœnix, etc., Co., the question has been again before the federal supreme court, and the doctrine of the cases upon which we relied for our decision limited, and in Great Western, etc., Co. v. Purdy, 162 U. S. 329, it is held that an order making a call or assessment upon all stockholders of a corporation who have not paid their shares in full is merely such a call as the directors might have made before the matter was brought within the court's jurisdiction, and is not a judgment against the particular stockholder, so as to be entitled to such full faith and credit, under the constitution and laws of the United States, and that in such action defendant is entitled to rely on any defense which he might have to an action upon the contract of subscription."

[1] Scovill v. Thayer, 105 U. S. 143; Hawkins v. Glenn, 131 U. S. 319–329; Lamb v. Lamb, 6 Biss. 420–424; Glenn v. Sexton, 68 Cal. 353; Great Western, etc., Co. v. Gray, 122 Ill. 630; Great Western, etc., Co. v. Loewenthal, 154 Ill. 261.

[2] Hawkins v. Glenn, 131 U. S. 319; Glenn v. Liggett, 135 U. S. 533; Glenn v. Marbury, 145 U. S. 499.

port to be a judgment against any one. * * * It did not merge the cause of action of the company against any stockholder on his contract of subscription, nor deprive him of the right when sued for an assessment to rely on any defense which he might have to an action upon that contract. In this action, therefore, brought by the receiver in the name of the company as authorized by the order of assessment to recover the sum supposed to be due from the defendant, he had the right to plead a release or payment or the statute of limitations or any other defense going to show that he was not liable upon his contract of subscription."

CHAPTER 20.

THE CONSTITUTIONAL AND STATUTORY LIABILITY OF STOCKHOLDERS.

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§ 558. **General statement.**—In most of the states the members of private corporations are now charged with an imposed

liability in addition to that which grows out of their contracts with the corporation. This liability must of course depend upon the constitutions and statutes, and there is so great diversity among these as to render it impracticable to attempt to state general rules applicable in all jurisdictions. The liabilities thus imposed may, however, be roughly classified as follows: (1) A joint and several liability as partners; (2) a joint and several liability as guarantors; and (3) a limited and several liability to be enforced absolutely or, more commonly, upon regular proceedings against the corporation proving ineffectual. The first class abrogates entirely the rule of limited liability and is governed by the law of partnership.[1] The member becomes a principal debtor.[2] Under the second class the liability is secondary and collateral to that of the corporation, and is governed in a general way by the rules of guaranty. Thus, any act on the part of the creditor which will release a guarantor will release a stockholder from his liability.[3] The liability under the third class is ordinarily limited to (a) an amount equal to the shares of capital stock held by the member; or (b) an amount equal to the ratio which the members' proportion of the capital stock bears to the entire corporation indebtedness. "The distinctive characteristic of this liability is that each member stands liable for a definite sum and no more, irrespective of the amount for which the others are liable. It is a several, unequal and limited liability as to which each member stands alone, except that, if he pays more than his proportion of the debts of the company, he may, as in other cases, have contribution from his fellow shareholders."[4]

§ 559. **Power of legislature to impose liability.**—There is no question as to the power of the legislature to impose a statu-

[1] See Corning v. McCullough, 1 N. Y. 47; Allen v. Sewall, 2 Wend. (N. Y.) 327, 6 Wend. 335; Moss v. Oakley, 2 Hill (N. Y.) 265.

[2] See Booth v. Dear, 96 Wis. 516, 71 N. W. Rep. 816.

[3] Sayles v. Brown, 40 Fed Rep. 8; Hanson v. Donkersley, 37 Mich. 184. See Harpold v. Stobart, 46 Ohio St. 397, 15 Am. St. Rep. 618, and Aultman's App., 98 Pa. St. 500.

[4] Thompson Liability of Shareholders, § 37. See Clarke v. Cold Spring, etc., Co. (Minn., 1894) 59 N. W. Rep. 632. As to the manner of proving who are stockholders, see § 471; Hinsdale Sav. Bank v. N. H. Banking Co., 59 Kan. 716, 68 Am. St. Rep. 391.

tory liability upon the stockholders of a corporation, if the power to alter and amend the corporate charter has been reserved,[1] and the limit of liability is not determined by the constitution.[2] If there is no such reservation, the liability can be imposed upon those only who become stockholders after the passage of the law. A constitutional provision imposing a liability does not impair the power of the legislature to impose an additional liability.[3] A liability beyond that imposed by the charter and contract of subscription can not be imposed by a by-law without the unanimous consent of the stockholders.[4]

§ 560. **Limitations by contract.**—A creditor may, by an express contract[5] at the time the debt was contracted, or by his conduct,[6] waive his right to proceed against stockholders for the collection of his debt. The only difficulty has been in proving the agreement. Evidence that at the time of the signing of the articles of association, and during the negotiations which resulted in their execution, it was verbally agreed among those who signed the articles and became stockholders that they should not be individually liable for corporate debts, is inadmissible because it tends to vary the terms implied by law of the articles of incorporation.[7] But the stockholder may show that at the time of the giving of certain notes by the corporation it was orally agreed between the payee and the corporation that

[1] Sleeper v. Goodwin, 67 Wis. 577, 31 N. W. Rep. 335; Ireland v. Palestine, etc., Co., 19 Ohio St. 369.

[2] Van Pelt v. Gardner, 54 Neb. 701. As to the rule where the power to alter or amend the charter has not been reserved, see Dow v. North., etc., R. Co., 67 N. H. 1; Gray v. Coffin, 9 Cush. (Mass.) 192.

[3] Allen v. Walsh, 25 Minn. 543.

[4] Trustees v. Flint, 13 Metc. (Mass.) 539. The court said: "It is not, in the opinion of the court, within the corporate powers conferred upon this and similar corporations, to impose upon their members by any such by-law any personal and individual liability to third persons beyond such as are specified in the charter or the general law of the commonwealth. Such a power would be liable to great abuse, and would subject every member of a corporation, however liberal its charter in excluding individual liability, to be made responsible for the entire indebtedness of the corporation by the act of those convened at a meeting of the corporation."

[5] United States v. Stanford, 70 Fed. Rep. 346; 44 U. S. App. 68; 17 C. C. A. 143; affirmed, 161 U. S. 412; Robinson v. Bidwell, 22 Cal. 379.

[6] Ohio, etc., Co. v. Merchants', etc., Co., 11 Humph. (Tenn.) 1, 53 Am. Dec. 742.

[7] Oswald v. Minneapolis Times Co., 65 Minn. 249.

there should be no personal liability on the part of the stockholders for the debt, although no reference was made to the agreement in the notes.[1] The court said:

"In terms, the notes promise only the payment of a sum of money by the company on a certain day. They have nothing to say about the defendants at all. If, then, the agreement is held to vary them in their legal effect, it must be on the ground that the statute which makes stockholders liable in certain cases makes that liability a term of the notes by implication. With regard to this it will be observed that the statute does not create a chartered partnership which remains a partnership and contracts as such, although granted certain charter powers. It does not make or leave the members primary contractors or debtors. It creates a corporation out and out, and then imposes a secondary and subsidiary liability upon the members 'for its (the corporation's) debts or contracts.' The liability of a member does not arise until after the contract has been broken, a judgment recovered upon it and execution returned unsatisfied. The corporation is the only promisor or debtor; it alone breaks the contract by its failure to pay, and it alone is sued. The liability of the members is no part of the original undertaking, but a consequence attached by the law to its breach. But the rule excluding evidence of oral agreements to vary a writing goes no farther than the writing goes. And at most the writing only expresses the obligation assumed by the party signing it. * * * The most obvious and natural view is, that the promise is the only thing which the writing has undertaken or purports to express, either in words or by legal implication. Certainly the writing

[1] Brown v. Eastern Slate Co., 134 Mass. 590. The court further said: "We have not considered whether the oral agreement is to be regarded as made with the corporation, or with these stockholders in person through the agency of the directors. It would seem to be possible to take it either way; the consideration in the former case being the delivery of the notes, in the latter the consent to issue them. But it is not necessary to decide the point, because, even taking it to have been the contract of the corporation, the plaintiff could not strike at the members of that corporation in a court of equity through and by means of a transaction which bound him not to do so."

does not extend to the remedies which the law will furnish for the collection of damages, even from the promisor himself, as is shown by the fact that they are governed by the *lex fori*, and *a fortiori*, not to the collateral statutory liability of third persons not parties to the writing."

§ 561. **Exceptions in favor of certain classes of corporations.**—Certain classes of corporations, such as those organized for manufacturing or mechanical purposes, are sometimes excepted from the operation of the statutes which impose personal liability upon the stockholders. The exception in favor of manufacturing corporations applies only to such as are organized for the purpose of carrying on an exclusively manufacturing business. If the articles of association state the purpose of conducting a manufacturing business, and also other kinds of business not incidental to or necessarily connected with the manufacturing business, the corporation is not within the exception, although it actually engages only in a manufacturing business.[1] So a corporation organized for "the manufacture, purchase, repair and sale" of agricultural instruments, which sells goods manufactured by others, is not a manufacturing corporation exclusively, and the stockholders are subject to the statutory liability.[2] Persons can not escape

[1] Arthur v. Willius, 44 Minn. 409; Densmore v. Shepard, 46 Minn. 54; First Nat'l Bank v. Winona, etc., Co., 58 Minn. 167, 59 N. W. Rep. 997; State v. Minnesota, etc., Co., 40 Minn. 213.

[2] In First Nat'l Bank v. Winona, etc., Co., 58 Minn. 167, 59 N. W. Rep. 997, the court said: "The principal point urged by appellants is that the stockholders of the defendant corporation are not liable, because it is exclusively a manufacturing corporation. It was organized under title 2, ch. 34, Gen. St. 1878, and the purposes for which it was incorporated are expressed in its articles of incorporation as follows: 'The general nature of its business shall be the manufacture, purchase, repair and sale of plows, cultivators, and other farming and agricultural implements of all kinds, the purchase and sale of all materials necessary or convenient in the prosecution of said business, and to take, own, hold, mortgage, lease and convey any and all real estate necessary or useful therein.' One of the findings of fact made by the court below on the trial is as follows: 'That in fact the actual business carried on by said plow company at all times since its organization, and intended by its incorporators to be carried on by it, was exclusively that of manufacturing plows and other agricultural implements, and the disposing of the

the constitutional liability by organizing as a manufacturing corporation when it is evident that the primary object of the organization is wholly foreign to manufacturing.[1] Mining is not a manufacturing business.[2] A "mechanical business," within a provision exempting manufacturing or mechanical corporations, means a business closely allied to or incidental to some manufacturing business, such as the mining of iron ore in connection with the manufacture of iron products.[3] But a

product of its manufacture, except that for a limited time it handled and sold on commission goods manufactured by other persons and corporations, in connection with, and for the purpose of, reducing the expenses of selling and handling its own product.' We are of the opinion that by its articles of incorporation this defendant is both a manufacturing and mercantile corporation. Such articles of incorporation provide for the 'purchase' and 'sale of plows, cultivators and other farming and agricultural implements of all kinds,' as well as for the 'manufacture,' 'repair,' and sale of those articles. In this respect the case is quite similar to that of Densmore v. Shepard, 46 Minn. 54, 48 N. W. Rep. 528, 681. See, also, Arthur v. Willius, 44 Minn. 409, 46 N. W. Rep. 851; Mohr v. Elevator Co., 40 Minn. 343, 41 N. W. Rep. 1074. The fact that the stockholders, as found by the court, did not intend to carry on anything but an exclusively manufacturing business, and that the corporation never did carry on any other business except such commission business, can make no difference. 'And if the corporation is organized for the purpose, as declared in the articles of association, of carrying on both a manufacturing business, and also some other kind of business not properly incidental to, or necessarily connected with, a manufacturing business, the mere fact that the corporation never exercised all of its powers, and never in fact engaged in or carried on anything but a manufacturing business, will not bring it within the constitutional exception.' Arthur v. Willius, 44 Minn. 409, 46 N. W. Rep. 851."

[1] State v. Minn., etc., Co., 40 Minn. 213; Mohr v. Minn., etc., Co., 40 Minn. 343.

[2] Byers v. Franklin Coal Co., 106 Mass. 131.

[3] Cowling v. Zenith, etc., Co., 65 Minn. 263, 33 L. R. A. 508. In considering the meaning of "mechanical" as used in the constitution the court said: "We are of the opinion that it was the intention of the makers of the constitution to exempt from liability the stockholders of corporations organized to carry on any such kind of mechanical business as is incidental to or closely allied with some kind of manufacturing business. Thus, a concern engaged in the business of manufacturing iron might well, as a mere extension of that business, or as incidental to it, mine its own ore, especially so if the manufacturing plant and the mines were in the same locality." An electric street railway company is not a "railroad" within the meaning of a statute which exempts the stockholders of railroad corporations from liability. Ferguson v. Sherman, 116 Cal. 169.

corporation organized in part for buying, selling, leasing and dealing in mineral lands is not organized for an exclusively manufacturing business so as to exempt the stockholders from liability.[1] The articles of association of a corporation stated that "its business shall be the manufacture of clothing of every description, and the sale of clothing so manufactured, and the transaction of all other business necessary and incidental to such manufacture and sale of clothing." The corporation was held to be a manufacturing corporation, and the mere fact that it engaged in some business not authorized by the articles of association did not render its stockholders liable for the corporate debts under the constitution.[2]

§ 562. **Repeal of statute—Rights of creditors.**—In all cases, the remedy by which a right is to be enforced is under the general control of the legislature, and may be modified or repealed if another reasonably adequate remedy is provided.[3] But the existing creditors of a corporation have a vested right in the existing contractual liability of the stockholders, of which they can not be deprived by a repeal of the statute.[4]

§ 563. **Constitutional provisions—When self-executing.**—Whether such provisions imposing liability upon the stock-

[1] Anderson v. Anderson, etc., Co., 65 Minn. 281, 33 L. R. A. 510.

[2] Nicollet Nat'l Bank v. Frisk-Turner Co., 71 Minn. 413.

[3] Fourth Nat'l Bank v. Francklyn, 120 U. S. 747. "Whether a given statute, changing the relation of debtor and creditor, reaches the contract or affects the remedy merely, has been undoubtedly the most perplexing question of constitutional interpretation which has arisen in this country. The supreme court of the United States, after a line of decisions in which the pendulum has oscillated very considerably (see Walker v. Whitehead, 16 Wall. (U. S.) 314, 317; Van Hoffman v. City of Quincy, 4 Wall. (U. S.) 535, 550, 552; Green v. Biddle, 8 Wheat. (U. S.) 1, 84; Sturges v. Crowninshield, 4 Wheat. (U. S.) 122, 200, 201; Mason v. Haile, 12 Wheat. (U. S.) 370, 378; Beers v. Haughton, 9 Pet. (U. S.) 329, 359), seems to have settled substantially upon the doctrine that the remedy does not apply to those who become creditors after the repeal. Ochiltree v. Railroad Co., 21 Wall. (U. S.) 249."

[4] Hawthorne v. Calef, 2 Wall. (U. S.) 10. See Brown v. Eastern State Co., 134 Mass. 590; Hope, etc., Co. v. Flynn, 38 Mo. 483, 90 Am. Dec. 438; Grand Rapids Sav. Bank v. Warren, 52 Mich. 557; Norris v. Wrenschall, 34 Md. 492. *Contra*, Coffin v. Rich, 45 Maine 507, 71 Am. Dec. 559.

holders are self-executing, or require legislative action to give them effect, depends upon the intention of the people by which they are adopted, as deduced from the language used. If such was the intention of the law-making power, constitutional provisions are self-executing. "A constitution," says Mr. Justice Mitchell,[1] "is but a higher form of statutory law, and it is entirely competent for the people, if they so desire, to incorporate into it self-executing enactments. These are much more common than formerly, the object being to put it beyond the power of the legislature to render them nugatory by refusing to enact legislation to carry them into effect. Prohibitory provisions in a constitution are usually self-executing to the extent that anything done in violation of them is void. But instances of affirmative self-executing provisions are numerous in almost every modern constitution."[2] If the language of the constitution is general and the extent of the liability not determined, legislation will be necessary.[3]

The Minnesota constitutional provision is self-executing and creates an individual liability on the part of the stockholder for corporate debts to an amount equal to the amount of stock held or owned by him.[4] The Kansas constitutional provision, over the construction of which there has been so much litigation, provides that "dues from corporations shall be secured by individual liability of the stockholders to an additional

[1] Willis v. Mabon, 48 Minn. 140; 31 Am. St. Rep. 626; Dupee v. Swigert, 127 Ill. 494; Fowler v. Lamson, 146 Ill. 472. Judge Thompson, after referring to the decision in Willis v. Mabon, 48 Minn. 140; 31 Am. St. Rep. 626, says: "The writer is content to refer for his statement of his own views upon the question to that admirable decision." Corps., § 3004. For decisions to the effect that constitutional provisions are not self-executing, see Graves v. Slaughter, 15 Pet. (U. S.) 449; Blakeman v. Benton, 9 Mo. App. 107; French v. Teschemaker, 24 Cal. 518; Larrabee v. Baldwin, 35 Cal. 155.

[2] For instances of this, see State v. Weston, 4 Neb. 216; Thomas v. Owens, 4 Md. 189; Reynolds v. Taylor, 43 Ala. 420; Miller v. Marx, 55 Ala. 322, and People v. Hoge, 55 Cal. 612.

[3] French v. Teschemaker, 24 Cal. 518; Morley v. Thayer, 3 Fed. Rep. 737; Jerman v. Benton, 79 Mo. 148; Bowie v. Lott, 24 La. Ann. 214.

[4] Art. 10, § 3, Const. Minn.; Willis v. Mabon, 48 Minn. 140, 31 Am. St. Rep. 626.

amount equal to the stock owned by each stockholder and such other means as shall be provided by law; but said individual liability shall not apply to railroad corporations, nor corporations for religious and charitable purposes."[1] Of this provision, the supreme court of Illinois said:[2] "That provision seemed to impose on the legislature the duty of securing dues from corporations, but limited the power and discretion of that body to the extent to which it could make stockholders liable. It is only in exceptional cases that constitutional provisions enforce themselves. Usually they must be supplemented by legislation to become operative. The intention of the instrument must ordinarily prevail, and in its ascertainment we must look at the consequences of a particular construction. * * * To treat the provision as self-operating would do violence to two leading principles of construction; by rejecting a clause of the instrument and giving it no force and effect, and holding an ambiguous clause self-executing when that clause is of the most doubtful construction. It is apparent from a consideration of the provision itself that legislation was contemplated as necessary to carry into effect and enable the remedy to be applied and give the intended security to the creditor, and the clause can not be treated or construed as self-operative." Of the same provision, the New York court said:[3] "We think it quite clear that the provision of the constitution referred to is not self-executing, and of itself creates no liability whatever. The language used plainly contemplates that legislation was necessary in order to make it effectual. It was intended simply to confer authority upon the legislature of that state to legislate upon the subject, and perhaps to impress upon that body the duty of securing the debts of corporations by imposing upon the stockholders an individual liability."

[1] Art. 12, § 2, Const. of Kansas.

[2] Tuttle v. Nat'l Bank of Republic, 161 Ill. 497, 34 L. R. A. 750; Bell v. Farwell, 176 Ill. 489, 68 Am. St. Rep. 194.

[3] Marshall v. Sherman, 148 N. Y. 9, 51 Am. St. Rep. 654, and note. See, also, Bank v. Lawrence (Mich.), 76 N. W. Rep. 105.

I. Nature of the Liability.

§ 564. **When contractual.**—The statutory liability of stockholders is ordinarily held to be contractual, although this will depend of course upon the language and purpose of the constitutional or statutory provision.[1] In Massachusetts, where the courts have been slow to enforce this liability, it was recently said:[2] "The obligation imposed by the statutes of Ohio upon the stockholders for the purpose of securing the payment of the debts of the corporation is *quasi ex contractu*. It must be taken that all persons who become stockholders in an Ohio corporation know the law under which the corporation is organized, and assent to the liability which that law imposes upon stockholders; and that all persons who deal with the corporation rely upon the liability of the stockholders as security for the payment of whatever debts may be due them from the corporation."

The supreme court of Pennsylvania expressed the opinion, but did not decide,[3] that the Kansas statute imposed a contractual liability, and the same conclusion was reached by the United States Circuit Court sitting in New Jersey.[4] In some states the liability is said to be merely "statutory," as distinguished from contractual or penal.[5] A liability imposed upon the stockholders, officers or agents of a corporation for dereliction of duty, as for a violation of the provisions of a statute, such as the requirement that annual reports of the condition of the corporation shall be made and published, is penal in its nature.[6] A joint and several liability imposed

[1] Bank v. Francklyn, 120 U. S. 747; Cushing v. Perot, 175 Pa. St. 66; 34 L. R. A. 737; Howell v. Manglesdorf & Co., 33 Kan. 194; Appeal of Aultmann, 98 Pa. St. 505; Rhodes v. U. S. Nat'l Bank, 24 U. S. App. 607; 34 L. R. A. 742; National Bank v. Whitman, 76 Fed. Rep. 697.

[2] Post & Co. v. Toledo, etc., R. Co., 144 Mass. 341; quoted in Hancock Nat'l Bank v. Ellis (Mass.), 42 L. R. A. 401.

[3] Cushing v. Perot, 175 Pa. St. 66. See also Bell v. Farwell (Ill.), 52 N. E. Rep. 346.

[4] Western Nat'l Bank v. Reckless, 96 Fed. Rep. 59.

[5] Rice v. Hosiery Co., 56 N. H. 114, 128; Marshall v. Sherman, 148 N. Y. 9; New Haven etc., Co. v. Linden Spring Co., 142 Mass. 349, 353.

[6] Merchants' Nat'l Bank v. N. W., etc., Co., 48 Minn. 349; Globe Pub. Co. v. State Bank (Neb.), 59 N. W.

upon the stockholders in an amount equal to the amount of their stock for all debts created before all the stock is paid in is contractual.[1] The liability imposed by the national banking act is contractual and survives against the personal representatives of the stockholder.[2] Whether the liability is primary or collateral depends upon the language of the statute. In California and other states having similar statutes, it is held to be primary and absolute, and the right of action consequently accrues against the stockholder and the corporation at the same time.[3]

§ 565. **When penal.**—A penal statute is an act by which a forfeiture is imposed for transgressing the provisions of a statute. It may be remedial in one part and penal in another. The effect and not the form of the statute is to be considered, and if its object is clearly to inflict a punishment on a party for doing what is prohibited, or failing to do what is commanded to be done, it is penal in its character.[4] Thus, a statute which requires the officials of a corporation to publish an annual statement of its affairs, and in the event of failing to do so makes the directors jointly and severally liable for all debts of the company, is penal. Such provisions are intended for the protection of creditors and the prevention of frauds upon the public in respect to the financial condition of the corporation. The liability is created by the statute and is in the nature of a penalty imposed for neglect of duty.[5]

Rep. 683; Diversey v. Smith, 103 Ill. 378.

[1] Flash v. Conn, 109 U. S. 371.

[2] Richmond v. Irons, 121 U. S. 27; Hencke v. Twomey, 58 Minn. 550.

[3] Davidson v. Rankin, 34 Cal. 503; Morrow v. Superior Court, 64 Cal. 383; Fuller v. Ledden, 87 Ill. 310; Stewart v. Lay, 45 Iowa 604.

[4] Diversey v. Smith, 103 Ill. 378; Globe, etc., Co. v. State Bank (Neb.), 59 N. W. Rep. 683; Huntington v. Attrill, 146 U. S. 657; Merchants', etc., Bank v. N. W. Mfg., etc., Co., 48 Minn. 349; Aylsworth v. Curtis, 19 R. I. 516, 61 Am. St. Rep. 785.

[5] Globe, etc., Co. v. State Bank, 41 Neb. 175, 27 L. R. A. 854; Bank v. Bliss, 35 N. Y. 412; Miller v. White, 50 N. Y. 137; Easterly v. Barber, 65 N. Y. 252; Knox v. Baldwin, 80 N. Y. 610; Veeder v. Baker, 83 N. Y. 156; Pier v. Hanmore, 86 N. Y. 95; Stokes v. Stickney, 96 N. Y. 323; Manufacturing Co. v. Beecher, 97 N. Y. 651; Godsden v. Woodward, 103 N. Y. 242; Sayles v. Brown, 40 Fed. Rep. 8. The above section of the New York statute was copied in Colorado and of it the court said: "This statute is in its nature penal. It describes a determinate penalty for neglect of a duty imposed

§ 566. **Survival of the right of action.**—Whether the right to proceed against a stockholder upon his statutory liability survives his death will depend upon the nature of the liability. If it is penal, it will not survive; if it is contractual, it survives, and may be enforced against the estate in the hands of his personal representative.[1] A New York statute provided that "in limited liability companies, all the stockholders shall be severally and individually liable to the creditors of the company in which they are stockholders, to an amount equal to the amount of stock held by them respectively, for all debts and contracts made by such company until the whole amount of capital stock fixed and limited by such company shall be paid in, and a certificate thereof has been made and recorded." The liability imposed by this statute was held to survive the death of the stockholder. "It is not," said the court,[2] "like the liability of a trustee for neglecting to make a report or for declaring dividends out of capital stock, or acts of a kindred character. These are breaches of duty on the part of the managing agents of the corporation for which the statute has made them liable, and this liability can not be said to rest upon or grow out of the contract. The liability of a stockholder in the present case is different. Upon becoming the owner of the stock he voluntarily assumes the

by law upon the trustees of a corporation organized under our general incorporation act. The amount of the forfeiture is measured by the aggregate debt contracted by the company. The liability is not founded upon contract but arises from misconduct in office." Gregory v. Bank, 3 Colo. 332; Larsen v. James (Colo.), 29 Pac. Rep. 183. Statutory provisions of similar character were held to be penal in Mitchell v. Hotchkiss, 48 Conn. 9; Steam Engine Co. v. Hubbard, 101 U. S. 188; Globe, etc., Co. v. The State Bank (Neb.), 59 N. W. Rep. 683; Derrickson v. Smith, 27 N. J. L. 166; Breitung v. Lindauer, 37 Mich. 217.

[1] Cochran v. Wiechers, 119 N. Y. 399, 29 N. Y. St. Rep. 388, 7 L. R. A. 553; Flash v. Conn, 109 U. S. 371; Richmond v. Irons, 121 U. S. 27. See Dane v. Dane, etc., Co., 14 Gray (Mass.) 488. The liability, however, is not of such a nature that a claim can be filed in the probate court against the estate of a deceased stockholder. It must first be reduced to judgment in the manner provided by the statute. Nolan v. Hazen, 44 Minn. 478.

[2] Cochran v. Wiechers, 119 N. Y. 399, 29 N. Y. St. Rep. 388, 7 L. R. A. 553.

obligation imposed by the statute, and the creditors of the corporation who trust it may be said to do so upon the faith of the statute which is part of the contract. The statutory obligation is inherent in and forms a part of every contract that the corporation makes with creditors, prior to the time that the certificate required by the statute is filed." It is settled that an action to recover a statutory penalty does not survive the death of the party liable.[1]

§ 567. **Liability of officers and directors.**—The liability imposed upon the officers or directors of a corporation for a failure to comply with some statutory requirement is commonly spoken of as penal. But, by the highest courts, it is held that this is true only in a limited sense, and not in that international sense which will prevent its enforcement in a foreign jurisdiction. The New York statute provided: "If any certificate or report made, or published notice given, by the officers of any such corporation shall be false in any material representation, all the officers who shall have signed the same shall be jointly and severally liable for all the debts of the corporation contracted while they are officers thereof." Under this statute a judgment was obtained against one of the directors in New York, and thereafter an action was commenced upon the judgment in Canada, where it was held that the action could not be maintained, as the liability was penal. The Privy Council, however, reversed this decision on the ground that the statute was not penal in the sense of international law.[2] It was admitted that the courts of no state execute the penal laws of another state. "But," said Lord Watson, "a proceeding, in order to come within the scope of this rule, must be in the nature of a suit in favor of the state whose law has been infringed." The same conclusion was shortly afterwards reached by the supreme court of the United States in a suit which grew out of the same facts.[3] In Illinois a lia-

[1] Chitty Plead., 1, 7th Am. Ed., 103; Hambly v. Trott, 1 Cowp. 372.

[2] Huntington v. Attrill, L. R. (1893) A. C. 150; 8 L. T. R. 341 (P. C. 1892).

[3] Huntington v. Attrill, 146 U. S. 657. See Fitzgerald v. Weidenbeck, 76 Fed. Rep. 695.

bility imposed upon the directors of an insurance company, which issued policies before the capital stock was fully paid in, and a certificate thereof recorded, was treated as a penalty.[1] The court said: "Whether all the capital, or all but a nominal sum, or whether but an insignificant amount of the capital has been collected and paid in, would obviously be unimportant inquiries. He is only required to show that he is a creditor of the company, that the defendant is a trustee or incorporator, and that the whole amount of the capital of the company has not been paid in, and a certificate thereof recorded. * * * The statute in effect says the thing shall not be done, and if it is done, the trustees and corporators shall be liable, etc. In all the cases referred to the statute says the thing may be done, and the stockholders, etc., shall be liable, either absolutely, or until some subsequent thing shall be done. In one case the liability is a consequence of violating the law, or suffering it to be violated; in the other, liability is incurred in strict compliance with the law. In short, in the one case the liability is for a wrong done —a tort; in the other it is upon contract. * * * The liability is not, in fact, to those alone who are injured, but exists equally where no actual injury has been done, as, for instance, where the corporation is abundantly able to pay all its debts; but the liability is for a wrong done to the public, which, presumably, to some extent is a wrong also to every creditor. * * * The liability is because of the wrong—*i. e.*, the failure to perform the duties enjoined by the statute, and not upon the contract of subscription."

II. Against Whom the Liability is Enforcible.

§ 568. **As to time of holding stock.**—No general rule can be stated applicable to all the states, as the question must be determined by the nature of the liability. It has been held, upon the theory of an original, primary liability, that the liability attaches to persons only who were stockholders at the time

[1] Diversey v. Smith, 103 Ill. 378. It will be noted that the liability was here imposed upon the officers of the corporation.

the debt was contracted.[1] Where the charter of a corporation provided that "each of the stockholders of said company shall be personally liable for the debts of said company to an amount equal to the amount of the capital stock held by such stockholder and no more," it was held that stockholders at a time when a debt of the corporation was contracted, and those who became stockholders before the debt was paid, were individually liable for the debts.[2] It is now settled in Minnesota that the liability attaches to those who own the stock at the time the action to enforce the liability is commenced.[3] Under the Michigan statute one who was a stockholder in an insolvent corporation, when labor was performed for it, is liable for the debt[4]. A prior bona fide transfer of the shares terminates the statutory liability,[5] even for the debts contracted while he was a stockholder.[6] Those who were stockholders when the debt

[1] Moss v. Oakley, 2 Hill (N. Y.) 265; reversed in 5 Denio (N. Y.) 567, where it was held that the liability attached to those who were stockholders when the suit was commenced. But see Williams v. Hanna, 40 Ind. 535.

[2] Gebhard v. Eastman, 7 Minn. 56, Gil. 40. The date of the debt is immaterial when the ownership of the stock was prior thereto and continued until after an action was brought against the corporation. Barron v. Burrill, 86 Maine 66. As to the liability of successive owners of shares, under a statute which imposes the liability for one year after a transfer of the shares, see Harper v. Carroll, 66 Minn. 487.

[3] Olson v. State Bank, 57 Minn. 552, 59 N. W. Rep. 635; First Nat'l Bank v. Winona, etc., Co., 58 Minn. 167, 59 N. W. Rep. 997. In Olson v. State Bank, 57 Minn. 552, 59 N. W. Rep. 635, the court said: "Does one who acquires stock in a banking corporation incur the statute liability in respect to corporate debts previously contracted, or does he incur it only in respect to debts subsequently contracted? The decisions of the courts in the different states seem at variance, the greater number holding that those who own the stock when the remedy is sought by the creditors—that is, when the action to enforce the liability is brought—are liable in respect to all the corporate debts, no matter whether contracted before or after they acquired their stock. The decisions in each state are based on the terms of the statute in each, as construed by the court; and as the terms of the statutes in the different states vary, but little aid is afforded by the decisions in other states." It is not material when the debt was contracted. Maine, etc., Co. v. Southern, etc., Co. (Maine), 43 Atl. Rep. 24; Rhode Island, etc., Co. v. Moulton, 82 Fed. Rep. 979.

[4] Macomber v. Wright, 108 Mich. 109, 65 N. W. Rep. 610; Kamp v. Wintermute, 107 Mich. 635.

[5] § 570, *supra;* Van Demark v. Barons, 52 Kan. 779; Rochester, etc., Co. v. Raymond, 158 N. Y. 576.

[6] Middletown Bank v. Magill, 5 Conn. 28; Dauchy v. Brown, 24 Vt.

was contracted and are stockholders when it is sought to be enforced, are liable, but not those who became such after the debt was contracted and transferred the shares before an action was brought to collect the debt.[1] It is sometimes provided that the stockholders shall remain liable for one year after the date of the transfer of his shares. The liability is then confined to such debts as were incurred before the transfer. The novation is complete and the transferrer released at the end of the year.[2]

§ 569. **Trustees, pledgees and executors.**—The statutory liability is intended to rest upon the owner of the shares, but by reason of the application of the doctrine of estoppel, it is sometimes imposed upon trustees, executors, agents and persons holding in a representative capacity. If the person in whose name the stock stands on the books of the company appears to be the owner, the appearance will be taken as the fact in favor of the creditors of the corporation. Thus, one who takes stock as collateral security for a debt, and has it transferred to him on the books of the corporation, is liable to the creditors of the corporation as a stockholder.[3] As this liability is based upon estoppel it exists only when there are facts which constitute an estoppel.[4] Thus, a pledgee of shares is not liable as

197. See Mason v. Alexander, 44 Ohio St. 318, 7 N. E. Rep. 435; Harpold v. Stobart, 46 Ohio St. 397, 21 N. E. Rep. 637; Sayles v. Bates, 15 R. I. 342.

[1] Sayles v. Bates, 15 R. I. 34; Barrick v. Gifford, 47 Ohio St. 180.

[2] Harper v. Carroll, 62 Minn. 152. As to the effect of transfer, see § 434, *supra*; Sprague v. Nat'l Bank, etc., 172 Ill. 149; Rhode Island, etc., Co. v. Moulton, 82 Fed. Rep. 979. A transfer may be made while the corporation is insolvent for the purpose of escaping liability. Peter v. Union, etc., Co., 56 Ohio St. 181. But see § 437, and Aultman's Appeal, 98 Pa. St. 505. One who assigns stock by a transfer not registered until after the assignment of the corporation is liable as a present stockholder. Harper v. Carroll, 66 Minn. 487.

[3] Pauly v. State Loan, etc., Co., 165 U. S. 606; State v. Bank of New England, 70 Minn. 398, 68 Am. St. Rep. 538, annotated; Nat'l Com. Bank v. McDonnell, 92 Ala. 387; National Bank v. Case, 99 U. S. 628; Goodwin v. Sleeper, 67 Wis. 577; Harper v. Carroll, 66 Minn. 487. See notes, 15 C. C. A. 133, 3 Am. St. Rep. 865, and 68 Am. St. Rep. 542. In McKim v. Glenn, 66 Md. 479, a broker who purchased stock for a client in his own name was held personally liable.

[4] Welles v. Larrabee, 36 Fed. Rep. 866.

a stockholder, if the shares have not been transferred to him or if the corporate books show that he holds the stock as collateral.[1] The same rule governs the liability of trustees[2] and executors.[3] Although a person holding stock in such a capacity may be liable to the extent of the trust estate,[4] he is not personally liable if the fact that he is not the beneficial owner appears on the corporate books. The estate of a deceased shareholder is liable for his share of the liabilities of the corporation, to the same extent as any other stockholder.[5] The manner of enforcing the liability will depend upon the statutes of the jurisdiction. After judgment it may be proved against the estate,[6] but before judgment it is a "contingent claim" and can not be thus proved.[7]

§ 570. **Unrecorded transfers—Liability of transferrer and transferee.**—It is generally stated in the books that until a transfer is recorded in the transfer books of the corporation, the transferee is not chargeable as a stockholder; that while he is bound to protect and indemnify his transferrer, he is not liable to the corporation or corporate creditors, and that the transferrer is not released from liability until the transfer is duly registered.[8] But "an examination of the authorities will

[1] Anderson v. Warehouse Co., 111 U. S. 479; Pauly v. State Loan, etc., Co., 56 Fed. Rep. 430, 58 Fed. Rep. 666, 7 C. C. A. 422; affirmed in 165 U. S. 606. Welles v. Larrabee, 36 Fed. Rep. 866; First Nat'l Bank v. Hingham Mfg. Co., 127 Mass. 563.

[2] Kerr v. Urie, 86 Md. 72, 38 L. R. A. 119.

[3] Welles v. Larrabee, 36 Fed. Rep. 866. In some states it is provided by statute that trustees and executors shall not be liable. Provisions of National Banking Act, Rev. St. U. S., § 5152, construed In re Bingham, 10 N. Y. Supp. 325, 32 N. Y. St. Rep. 782; Diven v. Lee, 36 N. Y. 302. Liability of estate of deceased non-resident stockholder. Grand Rapids Sav. Bank Appeal, 52 Mich. 557.

[4] Sayles v. Bates, 15 R. I. 342, 5 Atl. Rep. 497.

[5] Cochran v. Wiechers, 119 N. Y. 399, 7 L. R. A. 553; New England Com. Bank v. Newport Steam Factory, 6 R. I. 154, 75 Am. Dec. 688. See § 566, *supra*. If the title to the shares passes to the legatee he also takes the liability. Montgomery, etc., Assn. v. Robinson, 69 Ala. 413. As to the extent of the heirs' liability, see Payson v. Hadduck, 8 Biss. (C. C.) 293, and cases there cited.

[6] Nolan v. Hazen, 44 Minn. 478.

[7] Hospes v. Northwestern, etc., Co., 48 Minn. 174, 15 L. R. A. 470.

[8] If the transfer is waived by the corporation and the purchaser of the shares acts as a stockholder, he is liable as such to creditors. Upton v.

prove that this rule has not always been rigidly adhered to, but is subject to numerous exceptions and qualifications. It has, for example, been frequently held that where the corporation accepts the transferee as a stockholder, and he exercises any of the rights or accepts any of the benefits of a shareholder, he will be liable as such, although no transfer has been made on the books of the company. It has also been held that where the transferrer has done all he was required to do in the premises, but that through the negligence or fault of the company no transfer was entered on its books, the transferrer was released; applying the principle that a party can not take advantage of his own wrong, and that in equity that will be considered done which ought to be done."[1]

The owner of certain shares employed an auctioneer to sell them at public auction and they were bid off by a purchaser who paid the auctioneer for them and received from him the certificates of stock with a power of attorney duly executed in blank. The purchaser had been employed by the president of the bank to make the purchase for a customer of the bank who had deposited the money for the purpose in the bank. The certificate and power of attorney was delivered to the president, but no formal transfer was ever made on the books of the bank. The bank became insolvent, and after a receiver was appointed, an action was brought against the transferrer to collect an assessment under the statute. It was held that the responsibility of the transferrer ceased upon the surrender of the certificate to the bank and the delivery to its president of the power of attorney sufficient to effect and intended to effect, as the president knew, a transfer of the stock on the books of the bank.[2] But "where the seller delivers the stock certificate and power of attorney to the buyer, relying upon the promise

Burnham, 3 Biss. 431; Bell's Appeal, 115 Pa. St. 88, 2 Am. St. Rep. 532; Laing v. Burley, 101 Ill. 591. See Cormac v. Western, etc., Co., 77 Iowa 33. See also Sprague v. Nat'l Bank of America, 172 Ill. 149.

[1] Basting v. Northern, etc., Co., 61 Minn. 307 (an action against a transferee on a call), citing Whitney v. Butler, 118 U. S. 655; Ex parte Bagge, 13 Beav. 162; Young v. McKay, 50 Fed. Rep. 394; Chouteau Spring Co. v. Harris, 20 Mo. 382.

[2] Whitney v. Butler, 118 U. S. 655.

of the latter to have the necessary transfer made, or where the certificate and power of attorney are delivered to the bank without communicating to the officers the name of the buyer, the seller may well be held liable as a shareholder until, at least, he shall have done all that he reasonably can do to effect a transfer on the stock register."

But a transfer to the president of a bank as vendee of the shares is not sufficient to discharge the vendor under this rule.[1] In Ohio it is held that the seller must, at his peril, see that the transfer is made and his name removed from the books.[2]

III. The Debts for Which the Stockholders are Liable.

§ 571. **The debt of the corporation—Release.**—The right to proceed against a stockholder is dependent upon the existence of a debt due from the corporation to its creditors. In Minnesota it was held that the release of the debt and a judgment by a court discharging the debtor pursuant to the provisions of the insolvency law, released and discharged the stockholders from the personal liability imposed by the constitution.[3] Shortly after this decision the legislature amended the insolvency law by providing "that the release of any debtor under this act shall not operate to discharge any other party liable as surety, guarantor, or otherwise for the same debt,[4] and the court held that the word "otherwise," as here used, included stockholders who are liable for the debts of the corporation.[5]

§ 572. **Nature of the obligation.**—The imposed liability is generally for the debts of the corporation contracted or existing at a designated time. The word debt is generally construed to apply to obligations arising upon contract, and not to such as result from the torts of the corporation.[6] But under some

[1] Richmond v. Irons, 121 U. S. 27.

[2] Harpold v. Stobart, 46 Ohio St. 397; 15 Am. St. Rep. 618.

[3] Mohr v. Minn., etc., Co., 40 Minn. 343. Insolvency law of 1881 is applicable to private corporations. Tripp v. N. W. Nat'l Bank, 41 Minn. 400.

[4] Laws of 1889, ch. 30, § 1, amending ch. 148, Laws of 1881.

[5] Willis v. Mabon, 48 Minn. 140; Tripp v. N. W. Nat'l Bank, 41 Minn. 400. See Aultman's App., 98 Pa. St. 500.

[6] Child v. Boston, etc., Works, 137 Mass. 516, 50 Am. Rep. 328; Bohn

statutes a cause of action arising on tort is treated as a debt of the corporation.[1] The liability extends to the deficiency of debts secured by mortgages, as well as to unsecured debts.[2] A debt is not contracted by a corporation by the mere making of a contract for goods, before a delivery of the goods or a breach of the contract, under a statute making stockholders liable for debts contracted before the filing of a certificate.[3] Indebtedness maturing after the dissolution of a corporation, which

v. Brown, 33 Mich. 257; Doolittle v. Marsh, 11 Neb. 243. In Heacock v. Sherman, 14 Wend. (N. Y.) 59, it was held that the stockholders of an incorporated company were not individually liable for damages occasioned by a bridge built by the company being out of repair, although by the terms of the act of incorporation they were to be liable for "any demands against the company," the act contemplating liability only for damages arising *ex contractu*.

[1] Flenniken v. Marshall, 43 S. C. 80, 28 L. R. A. 402. In Rider v. Fritchey, 49 Ohio St. 285, an action to subject the stockholders to liability for a judgment obtained for personal injury was successful. The constitution provided that "dues from corporations shall be secured by such individual liability of stockholders," etc. The court said: "All concede that this is a remedial provision, and to hold that there must be applied to it the same test as if it were a penal law, is to hold that all remedial laws must be so construed, for every remedial law must of necessity be in derogation of the common law. * * * It must be manifest that the intent was to provide that those who derive advantage from the authority of the state given by our incorporation laws shall at the same time assume responsibility for the acts of the artificial creatures which they have called into being, affecting the rights of others. * * * It is conceded that if in a cause of action a tort can be treated as a 'debt,' the liability of the stockholders for it would follow. The affirmation of this is asserted and the following authorities are cited in its support: Carver v. Manufacturing Co., 2 Story 432; Milldam Foundry v. Hovey, 21 Pick. 417; Gray v. Bennett, 3 Met. 522; Smith v. Omans, 17 Wis. 395. To the contrary of this counsel for plaintiff in error cite Bohn v. Brown, 33 Mich. 257; Cable v. McCune, 26 Mo. 371; Doolittle v. Marsh, 11 Neb. 243; Heacock v. Sherman, 14 Wend. (N. Y.) 59; Archer v. Rose, 3 Brewster 264; Child v. Iron Works, 137 Mass. 516; Cook Stock and Stockholders, § 220; Morawetz, §§ 608, 613; Nanson v. Jacobs (Mo.), 6 S. W. Rep. 246; Evans v. Lewis, 30 Ohio St. 11; Crouch v. Gridley, 6 Hill 250; Kellogg v. Schuyler, 2 Denio 73, and Zimmer v. Schleehauf, 115 Mass. 52. * * * In conclusion, we are of the opinion that the word 'dues' should receive a beneficial construction, one which will include within its scope, as well a demand for unliquidated damages for a tort, as a claim for a debt arising upon a contract."

[2] Maine, etc., Co. v. Southern, etc., Co. (Maine), 43 Atl. Rep. 24.

[3] Wing & Evans v. Slater, 19 R. I. 597, 33 L. R. A. 566.

grew out of a contingent liability existing at the time of the dissolution, is within a statute[1] which imposes a liability on stockholders for the debts of the corporation.[2]

§ 573. **Debts due laborers and employes.**—Statutes often impose upon the shareholders a personal liability for debts due to its servants, laborers, employes and apprentices, who "usually look to the reward of their day's labor or services for immediate or present support, from whom the company does not expect credit, and to whom its future ability to pay is of no consequence."[3] Such provisions ordinarily apply only to those who perform manual labor,[4] and do not include such employes as foremen, superintendents and other officials.[5] But a superintendent, who performs manual labor, who is an employe and not an officer of the corporation, is a servant within the meaning of a statute which imposes an individual liability for debts due clerks, servants and laborers.[6] An attorney at law regularly employed on a salary is not an employe within a statute referring to "laborers, servants or employes."[7] One who makes a loan to a corporation to enable it to pay its workmen without intending to acquire the rights of the laborers to a preference can not afterward protect himself by taking an assignment from the workmen.[8] Such statutes impose a liability in addition to what remains unpaid upon their subscrip-

[1] 1 Kan. Gen. St. 1889, §§ 32, 44.

[2] Cottrell v. Manlove, 58 Kan. 405. As to the right to recover costs and receiver's expenses, see Harper v. Carroll, 66 Minn. 487. As to liability for debts when the stock of the corporation was fraudulently issued as fully paid up, see Wallace v. Carpenter, etc., Co., 70 Minn. 321, 68 Am. St. Rep. 530.

[3] Wakefield v. Fargo, 90 N. Y. 213, 217; Moyer v. Pennsylvania Slate Company, 71 Pa. St. 293; Harris v. Norvell, 1 Abb. N. Cas. 127; Sleeper v. Goodwin, 67 Wis. 577; Short v. Medberry, 29 Hun 39.

[4] Adams v. Goodrich, 55 Ga. 233.

[5] Coffin v. Reynolds, 37 N. Y. 640; Brockway v. Innes, 39 Mich. 47; Dukes v. Love, 97 Ind. 341. See Palmer v. Van Santvoord, 153 N. Y. 612.

[6] Sleeper v. Goodwin, 67 Wis. 577. A bookkeeper is not within the statute. Wakefield v. Fargo, 90 N. Y. 213. A traveling salesman is not a laborer. Jones v. Avery, 50 Mich. 326. A person employed at a salary by a mowing machine company to go from place to place and set up machines and to sell and solicit sales is an employe. Palmer v. Van Santvoord, 153 N. Y. 612.

[7] Bristor v. Smith, 158 N. Y. 157, 53 N. E. Rep. 42.

[8] Re Fair Hope, etc., Estate, 183 Pa. St. 96.

tions,[1] and the member is not relieved from this individual liability by a transfer of his shares.[2]

§ 574. **Creditors who are also stockholders and officers.**—The statutory liability of stockholders may be enforced for the benefit of creditors who are also stockholders and directors of the corporation. It was so held where it appeared that the directors and officers had become creditors of the corporation by loaning it money for the purpose of carrying on its business.[3] But it has been held that a director to whom the corporation is indebted for salary is not a creditor within the contemplation of such a statute.[4]

IV. Enforcement of the Liability.

§ 575. **At the domicile of the corporation.**—The manner of enforcing the liability of stockholders is so generally regulated by statute as to make it impractical to consider it in detail. In some states the creditor is authorized to bring an action at law against an individual stockholder, but probably the most common remedy is of an equitable nature, where all the stockholders and creditors are brought into court and the fund equitably divided.[5] The tendency is toward simplifying the procedure, and providing for an action or proceeding by the receiver of the corporation. The recent statutes and decisions of the state under consideration must be examined.[6]

§ 576. **Remedy against the corporation—Judgment.**—Where the liability is secondary, it is necessary that the creditor shall exhaust his remedies against the corporation before proceed-

[1] Milroy v. Spurr Mountain, etc., Co., 43 Mich. 231.

[2] Jackson v. Meek, 87 Tenn. 69, 10 Am. St. Rep. 620.

[3] Oswald v. Minneapolis Times Co., 65 Minn. 249. But see Potter v. Machine Co., 127 Mass. 592.

[4] McDowall v. Sheehan, 129 N. Y. 200. As to his remedy, see Tayer v. Tool Co., 4 Gray (Mass.) 75.

[5] See Booth v. Dear, 96 Wis. 516; Harper v. Carroll, 66 Minn. 487.

[6] For an illustration of what it is possible for an able and ingenious court to do with a blind and cumbrous statute, see the Minnesota cases construing ch. 76, Gen. Stat. 1878, from Allen v. Walsh, 25 Minn. 543, to Harper v. Carroll, 66 Minn. 487. Happily, much of it is swept away by Gen. Laws Minnesota 1899, ch. 272.

ing to enforce the statutory liability of the stockholders.[1] In the absence of a statute to the contrary, a judgment against the corporation and an execution thereon returned *nulla bona* is generally held to be a prerequisite to the right to proceed against the shareholder,[2] and this is sufficient evidence that the remedy against the corporation has been exhausted.[3] But if it appears that the corporation is notoriously insolvent,[4] or that there are no corporate assets to sequester, and the only relief obtainable is the enforcement of the statutory liability of the stockholders, an action for that purpose may be brought by a simple contract creditor.[5]

§ 577. **Judgment against the corporation—Conclusiveness.**— It may be taken as the settled law that a judgment against a corporation is conclusive upon the question of corporate indebtedness in a subsequent action against a stockholder of the corporation.[6] "It has been repeatedly held," says Judge Ald-

[1] Globe, etc., Co. v. State Bank, 41 Neb. 175, 27 L. R. A. 854. See Booth v. Dear, 96 Wis. 516; Cook Corp., § 219.

[2] National, etc., Co. v. Ballou, 146 U. S. 517; Swan, etc., Co. v. Frank, 148 U. S. 603; Fourth Nat'l Bank v. Francklyn, 120 U. S. 747; Libby v. Tobey, 82 Maine 397; Fowler v. Lamson, 146 Ill. 472; Allen v. Arnold, 18 R. I. 809; Remington v. Bay Co., 140 Mass. 494; Sturges v. Vanderbilt, 73 N. Y. 384; Rocky Mt. Bank v. Bliss, 89 N. Y. 338. But an adjudication in bankruptcy will render a judgment against the corporation unnecessary. Shellington v. Howland, 53 N. Y. 371. In Flash v. Conn, 109 U. S. 371, the court said: "The object of section 24 was to compel the creditor to exhaust the assets of the company before seeking to enforce the liability of the stockholder. When the declaration shows that this was done, and that a literal performance of the condition would have been vain and fruitless, the performance of the condition may well be held to have been excused."

[3] Baines v. Babcock, 95 Cal. 581. The return of an execution against the corporation "no property found" is sufficient to justify a suit against a stockholder under Kan. Gen. St. 1897, ch. 66, § 850, and in the absence of fraud on the part of the sheriff it can not be challenged by a stockholder. Thompson v. Pfeiffer (Kan.), 56 Pac. Rep. 763.

[4] Latimer v. Citizens' State Bank, 102 Iowa 162, 71 N. W. Rep. 225; Salt Lake, etc., Co. v. Tintic, etc., Co., 13 Utah 423, 45 Pac. Rep. 200. See also Sleeper v. Goodwin, 67 Wis. 577; Hirshfeld v. Bopp, 145 N. Y. 84.

[5] See Minneapolis Paper Co. v. Swinburne Co., 66 Minn. 378; Sturtevant-Larabee Co. v. Mast, etc., Co., 66 Minn. 437.

[6] Holland v. Duluth, etc., Co., 65 Minn. 324; Slee v. Bloom, 20 Johns. (N. Y.) 669; Farnum v. Ballard, etc., Shop, 12 Cush. (Mass.) 507; Came v. Brigham, 39 Maine 35; Nichols v.

rich,[1] "and the great weight of authority is that a judgment against a corporation in favor of a creditor without notice to a stockholder, conclusively establishes the fact of indebtedness, while in a comparatively few jurisdictions, it is treated as prima facie evidence only."[2]

§ 578. **By whom the liability is enforcible.**—No general rule can be stated as to who must enforce the statutory liability of stockholders. If the matter is not determined by the statute, it depends upon the nature of the liability and for whose benefit it is imposed. If the liability is regarded as an asset of the corporation, it passes to the receiver or assignee in insolvency of the corporation, and must be enforced by him for the benefit of the corporate estate.[3] The liability when contractual is sometimes held to be an asset of the corporation. "If the defendant's liability under the statute to the creditors of the corporation in which he is a stockholder is contractual—and it is only in that aspect that it can be enforced at all outside of Kansas—then it was like any other claim, an asset for the payment of the corporate debts, and as such the right to sue on it passed to the receiver. This is the general rule, so far as we are aware, and is so manifestly in accord-

Stevens (Mo.), 27 S. W. Rep. 613; Schertz v. First Nat'l Bank, 47 Ill. App. 124. See §§ 556, 587.

[1] Hale v. Hardon (C. C. A.), 95 Fed. Rep. 747. Where an action at law is brought in a federal court in New York to charge a stockholder in a Kansas corporation under the Kansas statute to the extent of his liability with a judgment against the corporation, it is sufficient to allege the recovery of the judgment, a return of execution unsatisfied, without averring the original debt, as the Kansas statute makes the judgment at least presumptive evidence; and it is immaterial that the New York courts in similar cases require the original debt to be pleaded, as the question is one of proof and not of pleading. Am., etc., Co. v. Woodworth, 79 Fed. Rep. 951. See generally Bank v. Francklyn, 120 U. S. 747; Hawkins v. Glenn, 131 U. S. 319; Glenn v. Liggett, 135 U.S. 533; McVicker v. Jones, 70 Fed. Rep. 754; Rhodes v. Bank, 66 Fed. Rep. 512, 13 C. C. A. 612; Bank v. Rindge, 57 Fed. Rep. 279; Borland v. Haven, 37 Fed. Rep. 394, 413; Glenn v. Springs, 26 Fed. Rep. 494.

[2] See Stephens v. Fox, 83 N. Y. 313.

[3] Sheafe v. Larimer, 79 Fed. Rep. 921; Howarth v. Ellwanger, 86 Fed. Rep. 54. The liability can not, under § 2933, Ind. R. St., be enforced by an assignee of the corporation. Runner v. Dwiggins, 147 Ind. 238, 36 L. R. A. 645.

ance with justice, as well as convenience, that in the absence of an express decision of the supreme court of Kansas to the contrary, we must presume that such is the law of that state."[1] The Massachusetts court says:[2] "We are unable to assent to the decision of the supreme court of Pennsylvania * * * that the liability of the defendant passed to the receivers of the corporation as an asset, because we think that the liability as created by the statute of Kansas is directly to the creditors, and can not be enforced by receivers in their own name or in the name of the corporation." Mr. Cook says that the claim against the stockholders "is not to be numbered among the assets of the corporation. * * * A receiver has no power to enforce such a liability."[3] High says:[4] "The authorities are not wholly reconcilable as to the right of a receiver of a corporation to maintain an action in behalf of its creditors to recover of shareholders an individual liability imposed by charter or statute upon stockholders for the protection of creditors." In Illinois it is said:[5] "The creditor stands on an independent platform above that of the receiver, having no concern with the corporation, and the stockholder is bound under the law to answer to him. The stockholder is not under the control or in the power of the receiver, but holds a fund, so to speak, out of which the creditors of the company may be paid." If the liability is directly to the creditors, it forms no part of the corporate assets and can not be enforced by the corporation or its representative.[6] Ordinarily, when the action is brought by

[1] Cushing v. Perot, 175 Pa. St. 66, 34 L. R. A. 737.

[2] Hancock Nat'l Bank v. Ellis, 172 Mass. 39, 42 L. R. A. 396. See former decision in 166 Mass. 414. First Nat'l Bank v. Hingham, etc., Co, 127 Mass. 563; Chamberlin v. Hugunot, etc., Co., 118 Mass. 532.

[3] Corps., § 218. In Runner v. Dwiggins, 147 Ind. 238, 36 L. R. A. 645, it was held that an assignee of an insolvent bank can not enforce the liability under Ind. Rev. St. 1894, § 2908, authorizing him to collect the "rights and credits" of the assignor.

[4] Receivers, § 317*a*.

[5] Arenz v. Weir, 89 Ill. 25. See Wincock v. Turpin, 96 Ill. 135; Munger v. Jacobson, 99 Ill. 349; Jacobson v. Allen, 20 Blatchf, 525; Billings v. Robinson, 94 N. Y. 415; Pfohl v. Simpson, 74 N. Y. 137. The Nebraska court not only imposes, but limits the liability.

[6] Van Pelt v. Gardner, 54 Neb. 701; Olsen v. Cook, 57 Minn. 522; Int.

a creditor against the stockholders, it must be for the benefit of all the creditors, and all the stockholders must be joined.[1]

§ 579. **Enforcement in foreign jurisdictions.**—The decisions with reference to the right to enforce the statutory liability of stockholders against stockholders who reside in a foreign jurisdiction are in a very unsatisfactory condition. It is stated in general terms that if the liability sought to be enforced is in the nature of contract, and is not opposed to the legislation or public policy of the state in which it is sought to enforce it, the courts of such state will entertain jurisdiction. It is admitted that a liability which is penal in its nature can not be enforced in a foreign jurisdiction. It is also generally conceded that the liability imposed by constitutions and statutes for the debts of a corporation is contractual, and

Trust Co. v. Loan, etc., Co. (Minn.), 65 N. W. Rep. 78. In re People's, etc., Co., 56 Minn. 180; Minneapolis, etc., Co. v. City Bank, 66 Minn. 441, 38 L. R. A. 415; Farnsworth v. Wood, 91 N. Y. 308. See Minneapolis, etc., Co. v. Swinburne Co., 66 Minn. 378; Strutevant-Larrabee Co. v. Mast, etc., Co., 66 Minn. 437. After the courts held that the statutory liability of stockholders in a bank could not be enforced by the receiver of the bank, the legislature enacted a statute authorizing such proceedings. See Gen. Laws 1897, ch. 341. The complicated and uncertain proceedings provided by ch. 76, Gen. Laws Minn., 1887, have now, at least in part, been superseded by ch. 272, Gen. Laws 1899, which provides a proceeding similar to that of the national banking act. The action against the stockholders may be prosecuted by the receiver, or if he fails to act, by a creditor for the benefit of all the creditors.

[1] Harper v. Carroll, 66 Minn. 487, 69 N. W. Rep. 610; Van Pelt v. Gardner, 54 Neb. 701. Under the Minnesota statute one creditor can not maintain an independent action at law against a single stockholder. Hanson v. Davidson (Minn.), 76 N.W. Rep. 254. In Western Nat'l Bank v. Reckless (C. C. N. J.), 96 Fed. Rep. 70, Mr. Justice Gray said: "We must assume the correctness of the statement in the declaration, in consideration of the demurrer, that under the Kansas constitution and laws, and the construction put upon them by the court of last resort in that state, an action at law by a single judgment creditor, lies against a single stockholder to enforce the liability created and provided for by said constitution and laws. The correctness of this statement is moreover established by an examination of the said provisions." See Mech. Sav. Bank v. Fidelity, etc., Co., 87 Fed. Rep. 113; Dexter v. Edmands, 89 Fed. Rep. 467. By a Kansas statute enacted in 1899, the right of action is now in the receiver. See Kisseberth v. Prescott, 95 Fed. Rep. 357.

therefore enforcible wherever the stockholder can be found, if there exists an appropriate remedy in such jurisdiction. But the courts of many of the states have been zealous to find technical difficulties in the way of a plaintiff who sought to collect his claim, and by a narrow and illiberal construction have practically deprived the creditors of a portion of the security, on the faith of which their debts were contracted. This has been particularly true of Massachusetts, New York[1] and

[1] The New York court of appeals is the only court which has had the courage to state the true reasons for the apparent judicial determination to protect their citizens from liability growing out of their foreign investments. In Marshall v. Sherman, 148 N. Y. 9, 34 L. R. A. 757, O'Brien, J., said: "There is still another aspect of the question which deserves attention, and it must be viewed in the light of notorious facts, which, though not appearing in the record, are matters of current history and common knowledge, to which we can not shut our eyes. Within recent years numerous business enterprises have been promoted in some of the western states, the money for the prosecution of which has been to a large extent borrowed here, either in the form of direct loans upon some kind of security, or by inducing many of our citizens to purchase stock in corporations organized for the purpose under local laws. Much of these investments, amounting to a vast sum in the aggregate, has been lost. This result is in some degree to be attributed to financial depression, and the consequent derangement of business, but in a much greater degree to the gross mismanagement and dishonesty of the managers and promoters. The funds thus procured have been used largely in furtherance of local and private interests, and in disregard of every prudent safeguard for the protection of the investors, and sometimes in defiance of every principle of common honesty. In some cases, when the managers well knew they were hopelessly involved, they continued to transact business, borrowing recklessly and pledging the assets in their possession or under their control. When the crash came these assets were sold by the pledgees, and, of course, sacrificed in many cases, leaving large deficiencies, which honest and prudent management could have converted into a surplus. A careful investigation of some of the disastrous failures of loan, investment, trust, land and mortgage companies, as well as banks and other corporations, will reveal this condition of things. It will not be difficult for speculators to purchase large claims against these defunct corporations at a very low price if they can be readily enforced here against stockholders who have made and lost investments in the stock." Any respect which this statement is entitled to must be reflected from the great court from which it emanated. It amounts to saying to the citizens of New York: You may invest your money in the stock of non-resident corporations under a contract by which you shall receive the benefits and share the burdens equally with

New Hampshire; although very recently the supreme court of Massachusetts[1] has reversed its former decisions and adopted a rule more consonant with justice and the comity which should exist between states of the Union. This departure is in line with the present tendency of judicial decisions, particularly in the federal courts.

§ 580. **Proceedings in the federal courts.**—The federal courts have been much more inclined to enforce the statutory liability of stockholders than the state courts. The right to enforce such liability presents a question of general law on which the federal courts follow their own precedents.[2] Thus, the federal court refused to follow the decision of the court of appeals of New York, which held that the liability under the Kansas statute could not be enforced in New York. "The declining of jurisdiction by those courts," said Wheeler, J.,[3] "can not, how-

your associates. If all goes well, and your agents and managers prove prudent and honest, the gain is yours. If you select dishonest or incapable managers of your business, and the enterprise fails, this court, although these matters are not pertinent in a case where a party is seeking to enforce a clear legal right, will see that all the loss shall fall upon your associates who reside in the foreign state. The foreign state will, through its comity, see that you secure the profits, if there are any; and we will protect you against the "injustice" of being required to pay your share of the losses. In commenting upon this decision, Judge Aldrich, in Hale v. Hardon, 95 Fed. Rep. 747, says: "We can not adopt this view for the reason that in judicial proceedings, except where the question of fraud or reckless management is made an issue, such considerations are contrary to principle, in the direction of repudiation, subversive of judicial right and of justice, and fraught with danger to the idea of permanent and uniform rule. A judicial result influenced by such considerations can stand neither the test of the rule of right nor of the requirements of prudence. In the next decade the stockholders may reside in the west and the creditors in the east. In the next case, the creditors may reside in the east as well as the stockholders; or, as in the present case, the creditors may be scattered over many states. It is not a question where the pecuniary interests are, but a question of right—a question whether an unquestioned liability shall be enforced outside of the parent forum after all has been done there that can be done, or whether the unquestionable right shall exist without a remedy."

[1] Hancock Nat'l Bank v. Ellis, 166 Mass. 414, and 172 Mass. 39; Stebbins v. Scott, 172 Miss. 356.

[2] Texas, etc., R. Co. v. Cox, 145 U. S. 593, 614; Flash v. Conn, 109 U. S. 371.

[3] Bank v. Whitman, 76 Fed. Rep. 697, 51 U. S. App. 536.

ever, take from this court what properly belongs to it, and the decision of what belongs to this must ultimately be determined by the supreme court of the United States. The decisions of that court must be followed here, as understood." From the recent federal decisions[1] the following general principles may be deduced. First, a contractual liability imposed upon stockholders by the laws of the corporate domicile is enforcible in any federal court wherein jurisdiction of the parties can be obtained. Second, the nature or character of the liability imposed, whether to the creditors severally and individually or in common, involves the interpretation of the law of the corporate domicile, and the interpretation by the courts of the domicile will be accepted by the federal courts. Third, where the laws of the corporate domicile provide a remedy for the enforcement of the right, it will be adopted and applied by the federal court, so far as consistent with their own rules of procedure. In a recent case in the court of appeals,[2] it was said: "We may well observe at the outset that for many years the steady trend of federal decision has been in the direction of upholding and enforcing extraterritorially this class of liabil-

[1] Fourth Nat'l Bank v. Francklyn, 120 U. S. 747; Flash v. Conn, 109 U. S. 371; Rhodes v. Bank, 24 U. S. App. (7th Cir.) 607, 66 Fed. Rep. 512, 34 L. R. A. 742; Whitman v. Bank, 83 Fed. Rep. 288, 28 C. C. A. 404 (2d Cir.); National Bank v. Whitman, 76 Fed. Rep. 697; American, etc., Co. v. Woodworth, 79 Fed. Rep. 951, 82 Fed. Rep. 269; McVickar v. Jones, 70 Fed. Rep. 954; Bank v. Rindge, 57 Fed. Rep. 279; Hale v. Hardon, 95 Fed. Rep. 747 (U. S. App., 1st Cir.); Brown v. Trail, 89 Fed. Rep. 641.

[2] Hale v. Hardon, 95 Fed. Rep. 747. Judge Aldrich said: "It does not seem necessary to refer to the numerous decisions of the supreme court and those of the various circuit courts of appeal, and of the circuit courts so often cited, which sustain the general proposition. We shall, therefore, only refer, in this connection, to the more recent cases in the U. S. courts, of Rhodes v. Bank, 24 U. S. App. 607; Whitman v. Bank, 28 C. C. A. 404; Elkhart Nat'l Bank v. Northwestern, etc., Co., 87 Fed. Rep. 252; Dexter v. Edmands, 89 Fed. Rep. 467, and to the more recent decisions of the state courts, as showing the present tendency of judicial decisions in such jurisdictions. Bagley v. Tyler, 43 Mo. App. 195; Guerney v. Moore, 131 Mo. 650; Ferguson v. Sherman, 116 Cal. 169; Cushing v. Perot, 175 Pa. St. 66; Hancock Nat'l Bank v. Ellis, 172 Mass. 39, and the admirable opinion of Chief Justice Field in that case, and to the exceedingly well-reasoned cases of Western Nat'l Bank of New York v. Lawrence (Mich.), 76 N. W. Rep. 105, and Bell v. Farwell, 176 Ill. 489, 52 N. E. Rep. 346."

ties according to the fair intendment of the local law in cases properly within the provisions thereof, except where enforcement would unreasonably interfere with local vested creditor's interests in states where enforcement is sought extraterritorially on grounds of comity, and perhaps in some cases, where such enforcement would offend the general public policy of the state, while among the courts of the states there has been a diminishing diversity of decisions upon questions growing out of such statutory liabilities." The federal courts sitting in a state are bound by a valid statute of the state which forbids the courts of the state to entertain actions of this character. But such a statute of New Jersey was held unconstitutional in so far as it applied to a creditor of a corporation of a foreign state who was given by its laws a personal right of action against any one of its stockholders for the collection of his debt. The creditor had, prior to the passage of the act, not merely as a matter of comity, but under the general principles of jurisprudence, a remedy for the enforcement of his contract in the courts of New Jersey of which he was deprived by the act.[1]

§ 581. **Decisions in various states—Massachusetts.**—Each state pursues what it regards as the best public policy in the matter of enforcing the liability imposed upon its citizens by the laws of other states. It is admitted in all cases that one who becomes a member of a foreign corporation subjects himself to the laws of the foreign state as regards his rights and liabilities. The enforcement of his liabilities must, however, be governed by the laws of his domicile unless personal service can be obtained upon him in the state of the corporate domicile. The federal courts enforce the stockholders' liability in cases within their jurisdiction, and there is a tendency in the same direction on the part of the state courts. The nature of the liability, as determined by the courts of the state of the corporate domicile, will generally be accepted as conclusive by the courts of other states, and a liability declared to be contractual will be enforced whenever jurisdiction over the person or property of the stock-

[1] Western Nat'l Bank v. Reckless, 96 Fed. Rep. 70.

holder can be obtained unless some question of procedure is involved. The diversity of decisions is so great that general rules can not be formulated, and the question must be determined by a careful study of the decisions of the state in question. Some of the states which have been most strict in refusing a remedy to the foreign creditor against the domestic stockholder have recently changed front and come into line with the federal courts. Thus in a comparatively recent case in Massachusetts the court said that "the question can hardly be considered as an open one in this commonwealth. This court has often declined to exercise jurisdiction to enforce a liability imposed upon stockholders in corporations established in other states under statutes of these states."[1] The decisions were placed upon the ground that "it is a suit against a foreign corporation which involves the relation between it and its stockholders and in which complete justice can only be done by the courts of the jurisdiction where the corporation was created."[2]

But in a later case, this court held that an action by a creditor to enforce the liability of a stockholder under the Kansas statute, is transitory, and may be brought in any court of general jurisdiction over similar actions in any state or country, where service can be made according to the law of the place.[3] The action was by a single judgment creditor against a single stockholder. In the course of an admirable decision, Chief Justice Field said: "The courts of Kansas, from the nature of the question, can never directly decide that the liability of a non-resident stockholder under the general statutes of Kansas is one that may be enforced in any court of general jurisdiction in any other state or country where per-

[1] Bank of North America v. Rindge, 154 Mass. 203; New Haven Nail Co. v. Linden Spring Co., 142 Mass. 349; Post & Co. v. Toledo, etc., R. Co., 144 Mass. 341, 59 Am. Rep. 86; Kansas, etc., Co. v. Topeka, etc., R. Co., 135 Mass. 34, 46 Am. Rep. 439; Halsey v. McLean, 12 Allen (Mass.) 438, 90 Am. Dec. 157; Penobscot, etc., R. Co. v. Bartlett, 12 Gray (Mass.) 244, 71 Am. Dec. 753; Erickson v. Nesmith, 4 Allen (Mass.) 233.

[2] Post & Co. v. Toledo, etc., R. Co., 144 Mass. 341, 59 Am. Rep. 86.

[3] Hancock Nat'l Bank v. Ellis, 172 Mass. 39, 42 L. R. A. 396, 55 Am. St. Rep. 414. See, also, Aldrich v. Anchor, etc., Coal Co., 24 Ore. 32, 41 Am. St. Rep. 831, and note.

sonal service can be made upon the stockholder. Only courts of other jurisdictions can decide that question. The courts of Kansas can only express an opinion to that effect if they entertain it in cases before them, as one of the reasons for the judgment they render in those cases. That opinion the supreme court of Kansas has expressed.[1] * * * The courts of the United States inferior to the supreme court have uniformly held that the liability under the statutes of Kansas which we are considering can be enforced against a stockholder in any state or district where he can properly be served with process.[2] These decisions are in accordance with the principles of the decisions of the supreme court of the United States with reference to statutes of other states somewhat similar to those of Kansas.[3] The decisions of state courts other than those of Kansas are not uniform upon the questions whether the statutory liability of a stockholder to creditors of the corporation under these statutes of Kansas can be enforced by a suit against the stockholder in any state where he resides and can be served with process."[4] After stating the rule that the action can not be maintained where the foreign statute creates as pecial remedy, the court said: "When the liability is distinctly imposed by statute upon the stockholders severally, it would be unfortunate if it should not be enforced against stockholders not resident within the state under whose laws the corporation has been

[1] Howell v. Manglesdorf, 33 Kan. 194.

[2] Whitman v. National Bank, 51 U. S. App. 536, 83 Fed. Rep. 288, 28 C. C. A. 404, affirming National Bank v. Whitman, 76 Fed. Rep. 697; Brown v. Trail, 89 Fed. Rep. 641; American, etc., Co. v. Woodworth, 79 Fed. Rep. 951, 82 Fed. Rep. 269; McVickar v. Jones, 70 Fed. Rep. 754; Rhodes v. U. S. Nat'l Bank, 66 Fed. Rep. 512, 13 C. C. A. 612, 34 L. R. A. 742; Bank, etc., v. Rindge, 57 Fed. Rep. 279. See Auer v. Lombard, 33 U. S. App. 438, 72 Fed. Rep. 209, 19 C. C. A. 72; Mechanics' Sav. Bank v. Fidelity, e'c., Co., 87 Fed. Rep. 113.

[3] Flash v. Conn, 109 U. S. 371; Huntington v. Attrill, 146 U. S. 657.

[4] In favor of the doctrine are Guerney v. Moore, 131 Mo. 650; Bagley v. Tyler, 43 Mo. App. 195. See Ferguson v. Sherman, 116 Cal. 169, 37 L. R. A. 622; Cushing v. Perot, 175 Pa. St. 66, 34 L. R. A. 737; Bell v. Farwell, 176 Ill. 489. *Contra* are Fowler v. Lamson, 146 Ill. 472, 37 Am. St. Rep. 163, and monographic note; Tuttle v. National Bank of the Republic, 161 Ill. 497, 34 L. R. A. 750. But see Bell v. Farwell, 176 Ill. 489, and Hancock Nat'l Bank v. Farnum (R. I. App. 1898), 40 Atl. Rep. 341.

established, for the reason that due process could not be served on them within the state, and the courts of the state where they reside would not take jurisdiction of suits to enforce the liability. It certainly concerns the due administration of justice that non-resident stockholders should be compelled by proceedings somewhere to perform the statutory obligations toward creditors of the corporation which they have assumed by becoming stockholders. * * * The courts of Kansas hold that the action must be against the stockholders severally, and not jointly. * * * The creditor can by action collect the amount of his judgment remaining unpaid of any stockholder 'to any extent equal to the amount of stock by him or her owned, together with any amount unpaid thereon.' The stockholder is discharged, as against all creditors of the corporation, when he has paid the debts of the corporation to this extent. We are unable to see in what manner the enforcement of these statutes by the courts of Massachusetts against stockholders resident here, at the instance of a creditor of the corporation, does any injustice to the citizens of Massachusetts." The court dissented from the view of the Pennsylvania court[1] that the liability passed to the receiver of the corporation as an asset and could be enforced by him.

§ 582. **Decisions in New Hampshire, New York and Illinois.**— In a late case in New Hampshire it was held that the liability imposed by the Kansas constitution and statutes could not be enforced in that state.[2] The court said: "The question of the enforcement of the laws of a foreign state is not a question of comity to that state, but of the power of the courts of the former. No court has any authority or power except such as is conferred upon it by the organic law or the statutes of the state that creates it." The liability was held to be "statutory" and not contractual. "The provision of the Kansas constitution referred to is plainly not self-executing and of itself creates no liability whatever. The only real basis of the plaintiff's right of action, legal, moral, or equitable, is the fiat of the Kansas legislature, for if

[1] Cushing v. Perot, 175 Pa. St. 66, 34 L. R. A. 737.

[2] Grippin, etc., Co. v. Laighton, (N. H.), 44 Atl. Rep. 538.

it be conceded (contrary to the fact as we understand it), what the courts of that state have directly held, that the relation as stockholder to creditors is contractual, the holding is properly to be regarded as a decision on general legal principles merely, and as such not binding upon us. * * * The alleged obligations of the defendant as a stockholder of the corporation are essentially different from those which arise in this state from that relation, and furthermore, the plaintiffs properly concede that their form of procedure should have been by an action at law. * * * Not only are the Kansas statutes relating to the liability of the stockholders and its enforcement radically different in theory and practice from ours, but there is no way in which they can be enforced here, so as to secure substantial justice according to the New Hampshire understanding and interpretations of that term. The practical difficulties are numerous, patent and insuperable."

New York also refuses to allow the liability imposed by the Kansas statute to be enforced in her courts.[1] A creditor, after obtaining a judgment against the insolvent corporation, and receiving part payment thereof from the receiver of the corporation, brought an action at law against a stockholder residing in New York to recover the balance. The complaint set out the provisions of the constitution and statutes of Kansas and the defendant demurred. It was held that the constitutional provision was not self-executing; that the statutory liability was not primary and contractual; and that the liability could only be enforced at the domicile of the corporation by the remedy provided by the statute. "If under any circumstances the action could be maintained in this jurisdiction it must be in such a form and by such modes of procedure as like liabilities created under our statutes are enforced against our citizens. * * * It is quite well established that in a case like this an action at law by a single creditor against a single stockholder for the recovery of a specific sum of money can not be maintained in our courts, under our statutes declaring the liability of stockholders. In

[1] Marshall v. Sherman, 148 N. Y. 9, 32 L. R. A. 757, 51 Am. St. Rep. 654.

such cases the liability must be enforced in equity in a suit brought by and in behalf of all the creditors against all the stockholders, wherein the amount of the liability and all the equities can be ascertained and adjusted. * * * It would, perhaps, be impossible to state the principle upon which the decision should rest without apparently coming in conflict with some of the numerous cases on the subject at some point. The great weight of authority, as will be seen, is against the right to maintain such an action." A later case in New York grew out of an attempt to enforce the liability under the laws of Washington. The court of the corporate domicile adjudged the corporation insolvent, appointed a receiver, ascertained the deficiency, ordered an assessment against the stockholders and directed the receiver to collect the assessments by suits in foreign jurisdictions where personal service could be obtained on the stockholders. The receiver represented all the creditors, and the fund resulting from the enforcement of the liability was for the benefit of all the creditors and became a part of the property in the hands of the corporation.[1] The receiver was allowed to maintain an action in New York against a resident stockholder.[2]

Illinois refused to enforce the same constitutional and statu-

[1] See Cole v. Satsop R. Co., 9 Wash. 487.

[2] Howarth v. Angle, 25 Misc. Rep. (N. Y.) 551. Affirmed in 39 App. Div. 151, where the court said: "The learned counsel for appellant calls our attention to Marshall v. Sherman, 148 N. Y. 9. That action was brought by a creditor of the Miltonvale State Bank, a corporation organized under the laws of Kansas, and the questions there considered arose upon a demurrer to the sufficiency of the complaint. In the course of the opinion delivered in that case, it was said that the statutes of Kansas provided for a special and peculiar remedy against the stockholders of a corporation created under the laws of that state, and that from the whole structure of them it is apparent that they were intended to operate and be enforced only within that jurisdiction. We think that case is distinguishable from the one in hand. In the case in hand the liability of the defendant has been judicially ascertained and declared, and the receiver represents all the creditors, and is seeking to maintain an action against the defendant upon his statutory liability as stockholder of the insolvent corporation. The course pursued by the receiver is like the course provided for the enforcement of liability of stockholders in this state."

tory provisions on similar ground. The proceedings were in the same form as in the New York case. It was held that the Kansas statute provided a special remedy for the enforcement of the liability, and that comity did not require the application of this remedy in another state which had a different and inconsistent method of procedure.[1] But in a late case, where the declaration alleged that under the laws of Kansas as interpreted by the highest court of that state, an action at law could be maintained by a single creditor against a single stockholder, it was held on demurrer that an action can be maintained in Illinois without first proceeding in equity in Kansas.[2] In the former case the court had determined the construction to be given the Kansas statute for itself.

In Michigan it was held that the liability under the same statute is individual to the creditor, is transitory and enforcible whenever service can be had.[3] In Pennsylvania it was said that the liability under the same statute was contractual and passed to a receiver of the corporation as an asset, and that the right to sue a stockholder in that state, if it existed, was in the receiver.[4]

§ 583. **Where a special statutory remedy is provided.**—It is the settled rule that a special remedy for the enforcement of the liability of the stockholder, provided by the laws of the state of the corporate domicile, will not on grounds of comity be enforced in the courts of another state which has a different and inconsistent procedure for the enforcement of such liabilities, when it will result in injustice to the citizens of the latter state.[5] There can be no objection to this general rule, if "injustice" is not so construed as to apply to the act of requiring the citizens of such state to comply with their contract obliga-

[1] Tuttle v. Nat'l Bank of the Republic, 161 Ill. 497.

[2] Bell v. Farwell, 176 Ill. 489, 52 N. E. Rep. 346, 68 Am. St. Rep. 194.

[3] Bank v. Lawrence (Mich.), 76 N. W. Rep. 105.

[4] Cushing v. Perot, 175 Pa. St. 66, 34 L. R. A. 737.

[5] May v. Black, 77 Wis. 101; First Nat'l Bank v. Gustin, etc., Co., 42 Minn. 327, 6 L. R. A. 676, 18 Am. St. Rep. 510; Hancock Nat'l Bank v. Ellis, 172 Mass. 39, 42 L. R. A. 396; Bank v. Rindge, 154 Mass. 203, 13 L. R. A. 56; Coffing v. Dodge, 167 Mass. 231.

tions. Where it was sought to enforce the liability under the Kansas constitution in Illinois the court said:[1] "In this case the right to recover rests on the statute of the state of Kansas alone, as the constitutional provision is not self-enforcible, and the liability is only attempted to be made resultant from legislation providing a special remedy and by the construction placed on that legislation by the courts of that state. The statutes of the state of Kansas have no force and effect in another state, and the enforcement of a remedy in this action in this state depends upon our express or tacit assent, which is usually expressed as the comity between states. The extent to which this principle of comity may proceed is subject to qualifications and restrictions which, in almost all cases, are to be determined by the particular sovereignty. A remedy special to a particular foreign state is not by any principle of comity enforcible here, and must be applied within the jurisdiction of the domicile of the corporation. * * * Each state determines its method of procedure in its courts and their jurisdictions. In this there is neither injustice nor hostility to a sister state. But it would be hostile to every principle of sovereignty to be compelled to import into this state the peculiar remedies and various special methods of procedure invented by the legislation of the various states. This principle has been variously recognized." This rule was recently applied in California[2] in an action brought to enforce the liability imposed by the statutes of Illinois, which made a transferrer of shares liable for the debts of the corporation to the extent of the amount unpaid on the stock and provided a special remedy for collecting the debt by way of garnishment.

§ 584. **Where no statutory remedy is provided.**—When the legislature creating a corporation declares that the stockhold-

[1] Tuttle v. National Bank of the Republic, 161 Ill. 497, 34 L. R. A. 750, citing Young v. Farwell, 139 Ill. 326; Patterson v. Lynde, 112 Ill. 196; May v. Black, 77 Wis. 101; Nimick v. Mingo, etc., Co., 25 W. Va. 184; Allen v. Walsh, 25 Minn. 543; Peck v. Miller, 39 Mich. 594; Barrick v. Gifford, 47 Ohio St. 180; Smith v. Huckabee, 53 Ala. 191; Terry v. Little, 101 U. S. 216; National Tube Works v. Ballou, 146 U. S. 517.

[2] Russell v. Pacific R. Co., 113 Cal. 258, 34 L. R. A. 747.

ers therein shall be individually liable for the debts of the corporation under certain circumstances, but fails to provide a method of procedure by which the liability shall be enforced, it is generally held that it can be enforced in another state, according to the procedure of the forum. In California it was recently said, in considering an Illinois statute:[1] "It is contended that the statute "merely creates a liability which is in the nature of a contract liability and which is enforcible wherever the stockholder can be found. The general rule upon this subject is very well established. Where a statute creates a right and prescribes a remedy for its enforcement, that remedy is exclusive. Where a liability is created which is not penal, and no remedy is prescribed, the liability may be enforced wherever the person is found. The procedure will, however, be entirely governed by the law of the forum. If the law creating a liability provides for a particular mode of enforcing it, the mode limits the liability. If it be a contract the parties here contracted with the understanding that they can be held liable in no other way,[2] and such a liability can not be enforced in another state."[3]

§ 585. **Ancillary proceedings.**—Where the statutes of the corporate domicile provide for proceedings of an equitable nature for the determination and enforcement of the statutory liability of stockholders, it is generally held that the remedy is exclusive, and that no proceedings can be maintained against the stockholders resident in a foreign jurisdiction. But in a recent case, the United States Court of Appeals in the First Circuit approves a proceeding which is very satisfactory, and, if adhered to, will render it comparatively easy to enforce such

[1] Russell v. Pacific R. Co., 113 Cal. 258, 34 L. R. A. 747. But see Marshall v. Sherman, 148 N. Y. 9.

[2] Fourth Nat'l Bank v. Francklyn, 120 U. S. 747.

[3] Young v. Farwell, 139 Ill. 326; Bank v. Rindge, 154 Mass. 203, 13 L. R. A. 56; Fowler v. Lamson, 146 Ill. 472; Jessup v. Carnegie, 80 N. Y. 441, 36 Am. Rep. 643; Erickson v. Nesmith, 4 Allen (Mass.) 233. See Hodgson v. Cheever, 8 Mo. App. 318; Paine v. Stewart, 33 Conn. 516; Aldrich v. Anchor, etc., Co., 24 Ore. 32; Rice v. Merrimac, etc., Co., 56 N. H. 114. But see Hancock Nat'l Bank v. Ellis, 172 Mass. 39, and Bell v. Farwell, 176 Ill. 489.

liability in the federal courts. Under the self-executing provision of the Minnesota constitution, it is held by the courts of the state that the liability is contractual, and that the cumbersome method provided for its enforcement is of an equitable nature. In proceedings under the statutes, a receiver was appointed to enforce the judgments entered against the stockholders, with authority to proceed against the non-resident stockholders not served in the original proceeding. This receiver was distinct from the receiver in the general insolvency proceedings. An action was commenced in the United States District Court in Pennsylvania *by one of the creditors* who had obtained judgment against the corporation in Minnesota in the sequestration proceedings. The corporation and all the stockholders residing in Pennsylvania were made defendants, but the action was dismissed on the ground that the corporation was a necessary defendant, and that the court had no jurisdiction over it. The decision was affirmed by the court of appeals, which, however, intimated an auxiliary bill might be the proper remedy in another jurisdiction.[1]

An action at law was also commenced *by the receiver* in the United States Circuit Court for Massachusetts against the stockholders within the jurisdiction of that court. It was brought on the theory that the stock liability created by the statute was in the nature of a trust fund primarily confided to the court of the jurisdiction of the corporate domicile; and that that court alone had jurisdiction to entertain the proceedings necessary to determine the necessity for and the extent to which the fund should be resorted to by creditors. Such an ancillary proceeding has no equitable features and was hence brought at law in the name of the receiver.[2] In this instance the court of the corporate domicile had said:[3] "As the amount and the par value of the stock issued and outstanding is a matter of record, and readily proven in any

[1] Elkhart Nat'l Bank v. Northwestern, etc., Co., 87 Fed. Rep. 252.

[2] See Auer v. Lombard, 72 Fed. Rep. 209; Alderson v. Dole, 74 Fed. Rep. 29.

[3] Hanson v. Davison (Minn.), 76 N. W. Rep. 254.

action, there is nothing to prevent the prosecution, after such decree is entered, of an ancillary action in another jurisdiction by the receiver appointed to collect and distribute the funds arising from the stockholder's liability in the general action, or by any other party or person who may be appointed by the court for the purpose, against any stockholder who is not made a party to the original action, to collect from him the amount of his liability on account of the debts of the corporation for the benefit of all the creditors."

It was held by the court of appeals of the first circuit that the non-resident stockholders were bound by the action of the Minnesota court, and that the plaintiff in his capacity as receiver for the creditors, might, in aid of the proceedings in Minnesota, maintain an action at law for such purpose in another jurisdiction. In an elaborate decision, marked by great breadth of thought, Judge Aldrich said,[1] with reference to the conclusiveness of the proceedings in the Minnesota court: "While we consider the cases[2] authorities to the extent that the stockholders are bound by the action of the corporation, or its successors in the exercise of corporate powers essential to the collection of debts, in respect to corporate matters, like requiring the payment of unpaid subscriptions to stock, which are part of the assets, and as to ascertainments in which the corporation is interested, like the ascertainment of the indebtedness of the corporation, we do not think they go to the length claimed by the plaintiff in this case, for the reason, as has already been said, the individual liability is not an asset of the corporation. Indeed, the Minnesota court did not undertake to render judgment upon the non-resident stockholders' liability, nor against the Minnesota stockholders upon their individual liability, otherwise than upon service, which is prerequisite to judgments *in personam*."[3]

[1] Hale v. Hardon (C. C. A.), 95 Fed. Rep. 747. See § 587.

[2] Hawkins v. Glenn, 131 U. S. 319; The Great West. Tel. Co. v. Purdy, 162 U. S. 329; Hanson v. Davison (Minn.), 76 N. W. Rep. 254; Reile v. Rundle, 103 U. S. 222.

[3] Pennoyer v. Neff, 95 U. S. 714; Hekking v. Pfaff, 91 Fed. Rep. 60, 50 U. S. App. 484.

§ 586. **Original proceedings in court of corporate domicile.**— Where the law of the corporate domicile provides an equitable proceeding for the enforcement of the stockholders' liability, and contemplates the creation of a fund out of which the creditors are to be paid, the courts of the corporate domicile must determine the questions which arise before it can be known whether it will be necessary to call upon the stockholders. In an Illinois case, where a creditor brought an action at law to enforce the liability imposed by the constitution of Kansas, it was held that the action could not be maintained.[1] The court said: "The important question to be here determined is whether the courts of this state will, in any form, take jurisdiction of a question arising as to the respective relations of creditors and stockholders of a corporation of another state, where a special remedy is provided by statute, before there is a determination by the courts of such state of the just proportion of the corporate indebtedness to be borne by solvent stockholders of such corporation. No decree of the courts of this state could result in taking an account and dissolving a corporation of another state. It is for the courts of that state to enter a decree stating the account, winding up the affairs of the corporation, and determining the relation of the stockholders, creditors and corporation to each other. When that question has been determined by the courts of that state, then, if it becomes necessary, the creditors, stockholders and the corporation, or its representative, may, as against stockholders who are domiciled here, appeal to the courts of this state, and have, as against such domiciled stockholders, adequate relief."

In a recent case in Wyoming the court said:[2] "Until the courts in Utah, in some appropriate proceeding, shall have judicially ascertained, and by decree determined, the amount of the deficiency for which the stockholders are responsible, it

[1] Tuttle v. National Bank of the Republic, 161 Ill. 497, 34 L. R. A. 750. See also Young v. Farwell, 139 Ill. 326; Hanson v. Davison (Minn.), 76 N. W. Rep. 254; National Bank v. Sayward, 86 Fed. Rep. 45.

[2] McLaughlin v. O'Neill (Wyo.), 51 Pac. Rep. 243-250. An action by the receiver.

is not perceived how any recovery can be had in this state, or any other, against a single stockholder."

In Massachusetts the court said:[1] "This court does not take jurisdiction of a suit to enforce the liability of stockholders in a foreign corporation, not because it would be a suit to enforce a penalty or a suit opposed to the policy of our laws, *but because it is a suit against a foreign corporation*, which involves the relation between it and its stockholders, and in which complete justice can only be done by the courts of the jurisdiction where the corporation was created. * * * If an assessment is to be laid upon the members or stockholders, or a contribution enforced from them, according to the law of the state under which the corporation is created, the courts of that state alone can afford complete and effectual judicial relief."

§ 587. **Conclusiveness of the decree of the court of the domicile.**—The decree of the court of the corporate domicile determining the relation between the corporation and its stockholders and creditors, the amount of the corporate debts, and the necessity for and the amount of the assessment, unless impeached for fraud, is conclusive and binding upon foreign stockholders who were not served with process within the jurisdiction and did not appear in the proceedings. The stockholders are represented by the corporation in the action, and the judgment is in effect against the stockholders in their corporate capacity. In principle there is no difference in this respect between an action to enforce an unpaid subscription and one to enforce a stockholder's liability.[2]

§ 588. **Rights of receiver in a foreign jurisdiction.**—Although under the laws of the corporate domicile it may be established that the receiver is the proper person to enforce the stockholder's liability, when he goes into the foreign jurisdiction he is liable to be confronted by the rule that a receiver can not maintain an action in a jurisdiction other than that of the court by

[1] Post & Co. v. Railroad, 144 Mass. 341. See § 582, *supra*.

[2] Hanson v. Davison (Minn.), 76 N. W. Rep. 254; Hale v. Hardon, 95 Fed. Rep. 747. See § 556, *supra*.

which he was appointed. This rule is generally said to be established and has recently been enforced for the purpose of preventing the enforcement of stockholders' liability.[1] Mr. High states the general rule, but says:[2] "It is thus apparent that the exceptions to the rule denying to receivers any extra-territorial right of action have become as well recognized as the rule itself, and the tendency of the courts is constantly toward an enlarged and more liberal policy in this regard. It is believed that the doctrine will ultimately be established giving to receivers the same rights of action in all the states of the Union with which they are invested in the state or jurisdiction in which they are appointed." A more recent writer says:[3] "The tendency of courts is in the direction of a liberal extension of the doctrine of interstate comity, and is against a narrow and provincial policy which would deny proper effect to judicial proceedings of sister states simply because they are foreign and not domestic." The exception referred to leaves the rule that *a receiver will be permitted to maintain an action in a foreign state when it will not interfere with the rights and privileges of the citizens of the state or contravene the policy of the laws of that state.* It remains somewhat a matter of favor discretionary with the court whose aid is invoked. As said in Alabama:[4] "In the absence of statutory regulations, the appointment and title of a receiver may be recognized and he may sue in the courts of another state, unless such suit works injustice or detriment to the citizens thereof, or contravenes the policy of its laws." The same rule[5] pre-

[1] Wyman v. Eaton, 107 Iowa 214, 43 L. R. A. 695. The rule was first established by Booth v. Clark, 17 How. (U. S.) 321. See comment upon this case in Hale v. Hardon, 95 Fed. Rep. 747.

[2] Receivers, § 241.

[3] Smith Receivers, § 169.

[4] Boulware v. Davis, 90 Ala. 207.

[5] Stoddard v. Linn, 159 N. Y. 265; Toronto Gen. T. Co. v. C., B. & Q. R. Co., 123 N. Y. 37; Matter of Waite, 99 N. Y. 433; Dyer v. Power, 39 N. Y. St. Rep. 136; Story v. Furman, 25 N. Y. 214; Runk v. St. John, 29 Barb. 585; Pugh v. Hurtt, 52 How. (Pr.) 22; Peters v. Foster, 10 N. Y. Supp. 389; Barclay v. Quicksilver, etc., Co., 6 Lans. 25. In Howarth v. Angle, 25 Misc. Rep. (N. Y.) 551 (39 App. Div. 151), it was held that where the court of a foreign state in which a corporation was organized, has declared the corporation insolvent, appointed a re-

vails in New York and in most of the states,[1] as well as in the federal courts.[2]

V. Miscellaneous Rights and Defenses.

§ 589. **The right of set-off.**—In actions brought by or on behalf of all the creditors of a corporation to enforce the common law liability of its stockholders, the stockholder can not, unless permitted by statute, avail himself of a counter claim or set-off he may have against the corporation.[3] If the liabil-

ceiver, and determined his right to sue, and the liability of the stockholders, and has directed an assessment for the deficiency to be levied upon them; and the assessment has been levied, and the receiver has been directed by the foreign court to sue such stockholders as have refused to pay the assessment, he, as receiver, may, where no rights of domestic stockholders are concerned, maintain an action in the courts of New York against the resident stockholders to recover the unpaid assessment; and their liability is to be determined by the law of the state under which they became stockholdholders. In distinguishing the case of Marshall v. Sherman, 148 N. Y. 9, the court said: "The stockholders' liability created by the statute of Kansas can not in any event be enforced by an action at law by a single creditor against a single stockholder for the recovery of a specific sum of money in the state of New York, in which state the stockholders' statutory liability can be enforced only by a suit in equity, brought by or in behalf of all the creditors against the stockholders, wherein the amount of the liability can be ascertained and adjusted. Here the liability of each of the defendants has been ascertained and adjusted, and the action is by the receiver representing all the stockholders, and the only party under the laws of the state of Washington who can maintain an action against the defendants upon their statutory liability as stockholders in the insolvent corporation." Under the Washington statute the liability can be enforced only in equity. See Wilson v. Book, 13 Wash. 676.

[1] Bagby v. A. M. & O. R. Co., 86 Pa. St. 291; Metzner v. Bauer, 98 Ind. 425; Cooke v. Town of Orange, 48 Conn. 401; Lycoming, etc., Co. v. Wright, 55 Vt. 526.

[2] Peck v. Elliott (C. C. A.), 79 Fed. Rep. 10; Schultz v. Insurance Co., 77 Fed. Rep. 375 (C. C. A.), 80 Fed. Rep. 337; Kennedy v. Gibson, 8 Wall. (U. S.) 498; Keyser v. Hitz, 133 U. S. 138; Casey v. Galli, 94 U. S. 673. For the different kinds of receivers, see Hale v. Hardon, 95 Fed. Rep. 747; Relfe v. Rundle, 103 U. S. 222; Davis v. Gray, 16 Wall. 203, 209.

[3] Thompson v. Reno Sav. Bank, 19 Nev. 103; 3 Am. St. Rep. 797, ann. In re Empire City Bank, 18 N. Y. 199; Bissit v. Kentucky River Nav. Co., 15 Fed. Rep. 353; Wheeler v. Millar, 90 N. Y. 353; Tama Water Power Co. v. Hopkins, 79 Iowa 653; Shickle v. Watts, 94 Mo. 410; Mathis v. Pridham (Tex. 1894), 20 S. W. Rep. 1015; Singer, etc., Co. v. Given, 61 Iowa 93; Boulton Carbon Co. v. Mills, 78 Iowa 460; Thebus v. Smiley, 110 Ill. 316.

ity is on a contract of subscription he must pay what is due and share ratably with the other creditors. Where it was attempted to offset a debt against such a liability the court said: "The debt which appellant owed for his stock was a trust fund devoted to the payment of all the creditors of the company. As soon as the company became insolvent, and this fact became known to the appellant, the right of set-off for an ordinary debt to its full amount ceased. It became a fund belonging equally in equity to all the creditors, and could not be appropriated by the debtor to the exclusive payment of his own claim."[1] But the creditors can not, after insolvency, in the absence of fraud, question a set-off which was allowed by the corporation while it was a going concern.[2] Whether the stockholder can set off a claim against the corporation in a proceeding to enforce his additional or strictly statutory liability, depends upon the nature of the liability created by the particular statute. If it is of such a nature that any creditor can maintain an independent action against any stockholder to enforce a several and original liability, the stockholder may set off debts due him from the corporation.[3] If the stockholder purchases debts against the corporation, after he knows of its insolvency, he can have only the amount he paid therefor set off against his liability.[4] But if the object of the statute is to create a fund from which the creditors are to be paid ratably, the shareholder must "contribute his proportion thereto, and then come in with other creditors in the distribution of the corporate assets."[5] The demands of the

[1] Sawyer v. Hoag, 17 Wall. (U. S.) 610. But see Saving Bank v. Butchers', etc., Bank, 130 Mo. 155.

[2] Goodwin v. McGehee, 15 Ala. 232; Thompson v. Meisser, 108 Ill. 359; Paine v. Central Vermont R. Co., 118 U. S. 152.

[3] Coquard v. Prendergast, 35 Mo. App. 237; Wheeler v. Millar, 90 N. Y. 353; Jerman v. Benton, 79 Mo. 148; Boyd v. Hall, 56 Ga. 563; Thompson v. Meisser, 108 Ill. 359.

[4] Thompson v. Meisser, 108 Ill. 359; Balch v. Wilson, 25 Minn. 299; Bulkley v. Whitcomb, 121 N. Y. 107. In Abbey v. Long, 44 Kan. 688, it was held that they could be set off for their face value.

[5] In re Empire City Bank, 18 N. Y. 199; Thompson v. Meisser, 108 Ill. 359; Weber v. Fickey, 47 Md. 196; Witters v. Sowles, 32 Fed. Rep. 130; Thebus v. Smiley, 110 Ill. 316.

stockholders individually can not be interposed as equitable set-offs to a demand against the corporation, although the corporation is insolvent.[1]

§ 590. **Statute of limitations.**—The nature of the liability necessarily determines the application of the statute of limitations. Where the liability is primary and the obligation rests upon the stockholder from the time the debt is contracted the statute of limitations begins to run at the time the debt becomes due.[2] But where the obligation is in the nature of a surety, or is made dependent upon the insolvency of the corporation, the statute begins to run from the time this is determined. If the liability is penal in its nature, as that imposed by a statute upon directors who violate its provisions,[3] it is governed by the section of the statute of limitations relating to penalties and forfeitures.[4] The statutory limitation of six years upon a liability created by statute other than that upon a penalty or forfeiture, applies to the double liability of stockholders for the debts of corporations.[5]

The statute does not begin to run until the creditor acquires the right to sue the stockholder. Hence, when it is necessary to acquire judgment against the corporation the statute begins to run from the time of the return of an execution unsatisfied.[6] It was recently held in New York that the statute did not begin to run as against a foreign receiver in favor of a resident stockholder until the assets had been marshalled and the deficiency ascertained.[7]

[1] Gallagher v. Germania Brewing Co., 53 Minn. 214.

[2] Schalucky v. Field, 124 Ill. 617; Hyman v. Coleman, 82 Cal. 650.

[3] Patterson v. Stewart, 41 Minn. 84.

[4] Merchants' Nat'l Bank v. Northwestern, etc., Co., 48 Minn. 349; Merchants' Bank v. Bliss, 35 N. Y. 412; Wiles v. Suydam, 64 N. Y. 173.

[5] Merchants' Nat'l Bank v. Northwestern, etc., Co., 48 Minn. 349.

[6] Taylor v. Bowker, 111 U. S. 110; Younglove v. Lime Co., 49 Ohio St. 663.

[7] Howarth v. Angle, 25 Misc. Rep. (N. Y.) 551. Whether the liability is governed by the statute of the corporate domicile or of the *lex fori*, see Hobbs v. Nat'l Bank of Com., 96 Fed. Rep. 396.

§ 591. **Contribution among stockholders.**—Where the statutory liability is joint and several and in the nature of contract, a stockholder who is required to pay more than his proportion is entitled to contribution from the other stockholders.[1] There can be no contribution if the liability is penal.[2] Unless otherwise provided by statute, the remedy is by a suit in equity.[3]

[1] Harper v. Carroll, 66 Minn. 487; Wincock v. Turpin, 96 Ill. 135; Allen v. Fairbanks, 40 Fed. 188, 45 Fed. 445.

[2] Sayles v. Brown, 40 Fed. 8.

[3] O'Reilly v. Bard, 105 Pa. St. 569.

CHAPTER 21.

INSOLVENCY AND DISSOLUTION.[1]

§ 592. Manner of dissolution.
593. Impairment of contracts.
594. Expiration of term of existence.
595. Dissolution by legislative act.
596. Surrender of charter.
597. Forfeiture of charter.
598. Loss of integral part.
599. Statutory methods of dissolution—By the state.
600. Voluntary liquidation.
601. Statutory provisions for a temporary continuance of the corporation.
602. Insolvency, sale or loss of property—Abandonment of business.
603. Powers of a court of equity.
604. Proceedings by state.
605. Effect of dissolution, generally.
606. Effect upon corporate debts and assets.

§ 592. **Manner of dissolution.**—The dissolution of a corporation is that condition of law and fact which ends the capacity of the body corporate to act as such and necessitates a final liquidation and extinguishment of all the legal relations subsisting in respect of the corporate enterprise.[2] A dissolution may be effected (1) by the expiration of the statutory period of its existence, (2) an act of the legislature under a reserved power to repeal, (3) the surrender of the charter with the consent of the state, (4) the forfeiture of the charter for misuse or nonuse of its powers, (5) the loss of an integral part, without whose existence the functions of the corporation can not be exercised, and (6) compliance with whatever statutory requirements may exist in order to effect a voluntary dissolution.[3]

[1] See Wilgus' Cases, particularly Boston Glass Mfg. Co. v. Langdon, 24 Pick. (Mass.) 49; Higgins v. Downward, 8 Houst. (Del.) 227; Louisville Banking Co. v. Eisenman, 94 Ky. 83; Bradley v. Reppell, 133 Mo. 545; Brooklyn Steam T. Co. v. Brooklyn, 78 N. Y. 524; McGinty v. Athol R. Co., 155 Mass. 183; Philips v. Wickham, 1 Paige Ch. (N. Y.) 590; Mechanics' Bank v. Heard, 37 Ga. 401; Wilson v. Proprietors, etc., 9 R. I. 590; Merchants' & P. Line v. Wagner, 71 Ala. 581.

[2] Taylor Priv. Corp., § 429.

[3] 2 Kyd Corp., 447; 2 Kent Com. (13th ed.), 306; 1 Bl. Com., 485; Angell & Ames Corp., p. 501; Oakes v. Hill, 14 Pick. (Mass.) 442. See generally notes to 7 Am. St. Rep. 684, 717; 57 Am. St. Rep. 76; 12 Am. Dec. 239; 40 Am. Dec. 737; 99 Am. Dec. 336.

§ 593. **Impairment of contracts.**—Parties deal with corporations subject to the possibility of losses arising from their dissolution,[1] and the fact that a forfeiture of the charter will impair outstanding contracts does not affect the power of the court to decree such forfeiture.[2] Laws authorizing the dissolution of corporations "enter directly into the contract, and as corporations have the power to dissolve themselves or consent to a forfeiture of corporate franchises, all persons must be regarded as having contracted upon the hypothesis of the existence and possible exercise of this power."[3] A court of equity will not, in the absence of fraud, at the instance of creditors who have levied an attachment on the property of the corporation, restrain the stockholders from dissolving the corporation.[4] But a dissolution does not destroy the obligation of the company's contracts, as the equitable rights of creditors survive the act of dissolution and attach to the assets and property of the corporation in the hands of its liquidators.[5]

§ 594. **Expiration of term of existence.**—The original idea of a corporation involved perpetuity, but under modern statutes the life of a corporation is universally limited to a term of years with possibly a provision for renewal. By the weight of authority a corporation is *ipso facto* dissolved by the expiration of this period,[6] although there are some decisions to the effect that it continues to exist as a *de facto* corporation and that its exercise of corporate franchises can be questioned only by the state in direct proceedings.[7]

[1] Read v. Frankfort Bank, 23 Maine 318. As to the remedy after dissolution, see Schlieder v. Dielman (La.), 10 So. Rep. 934.

[2] Mumma v. Potomac Co., 8 Pet. (U. S.) 281; Wash., etc., Co. v. State, 19 Md. 239.

[3] State v. Gaslight Co., 5 Rob. (La.) 539; Schlieder v. Dielman (La. 1892), 10 So. Rep. 934; Railroad Co. v. State, 29 Ala. 573; Green's Brice Ultra Vires, §§ 138, 435.

[4] Cleveland City, etc., Co. v. Taylor Bros., etc., Co., 54 Fed. Rep. 85, distinguishing Fisk v. Railroad Co., 10 Blatchf. 518.

[5] People v. O'Brien, 111 N. Y. 1; Morawetz Priv. Corp., II, § 1035; Curran v. Arkansas, 15 How. (U. S.) 304.

[6] § 597, *infra*. Bradley v. Reppell, 133 Mo. 545, 54 Am. St. R. 685, 32 S.W. Rep. 645, Wilgus' Cases; Sturges v. Vanderbilt, 73 N. Y. 384.

[7] May be sued for a tort after its charter has expired. Miller v. Coal Co., 31 W. Va. 836. See Bushnell v. Machine Co., 138 Ill. 67. As to the term of existence, see § 70, *supra*;

§ 595. **Dissolution by legislative act.**—In the United States a corporation can not be dissolved by an act of the legislature without the consent of the corporators, unless the power was reserved at the time the charter was granted.[1] A repeal of the charter pursuant to an unconditional power reserved by the state is effective without a judicial decree when it clearly appears from the statute that such was the legislative intent.[2] Where the dissolution is to take place upon the happening of some contingency, the legislature may provide that the dissolution shall result without a judicial decree.[3] But unless such clearly appears to have been the legislative intent, a decree of forfeiture is necessary.[4] "The better opinion would seem to be that for most purposes the happening of the contingency upon which the corporation is to cease should also be judicially declared."[5] Generally this is necessary.[6] "Upon the absolute repeal of a charter by the legislature acting within the limits of constitutional authority the corporation ceases to exist and no judgment can afterwards be rendered against it in an action at law.[7] But such repeal does not impair the obligation of contracts made by the corporation with other parties during its existence, or prevent its creditors or stockholders from asserting their rights against its property in a court of chancery in accordance with the reasonable regulations of the legislature or with the general principles and practice of equity."[8]

§ 596. **Surrender of charter.**—A corporation may be dissolved by the voluntary surrender of the charter and its acceptance by the state. As said by the supreme court of Massachusetts: "Charters are in many respects compacts between the government and the corporators. And as the former can

State v. Hannibal, etc., Road Co., 138 Mo. 332, 36 L. R. A. 457.

[1] § 99, *supra*. Bruffett v. Great Western R. Co., 25 Ill. 310.

[2] Sturges v. Vanderbilt, 73 N. Y. 384; Terry v. Merchants', etc., Bank, 66 Ga. 177.

[3] In re Brooklyn, etc., R. Co., 75 N. Y. 335.

[4] LaGrange, etc., R. Co. v. Rainey, 7 Coldw. (Tenn.) 420.

[5] Taylor Priv. Corp., § 432; Flint & Fentonville Plank Road Co. v. Woodhull, 25 Mich. 99, Wilgus' Cases.

[6] Kincaid v. Dwinelle, 59 N. Y. 548; Moore v. Schoppert, 22 W. Va. 282.

[7] § 593. Marion, etc., Co. v. Perry, 74 Fed. Rep. 425, 41 U. S. App. 14, 33 L. R. A. 252.

[8] Thornton v. Railroad Co., 123 Mass. 32.

not deprive the latter of their franchise in violation of the compact, so the latter can not put an end to the compact without the consent of the former. It is equally obligatory on both parties. The surrender of a charter can only be made by some formal solemn act of the corporation; and it will be of no avail until accepted by the government. There must be the same agreement of the parties to dissolve that there was to form a contract. It is the acceptance which gives efficacy to the surrender."[1] But, as said by Mr. Taylor:[2] "The present applicability of the preceding citations to stock corporations is somewhat doubtful. Formerly corporations usually received special charters; but now stock corporations at least are almost universally organized under general enabling acts. A mode of dissolution is ordinarily provided; and if no such provision exists, the most experienced legal adviser might be puzzled to advise how an acceptance of the surrender of franchises could be brought about unless by lobbying a special bill through the legislature. Besides, the idea of the necessity of the acceptance of a surrender of franchises on the part of the authority granting them seems intimately connected with the old doctrine, now certainly a thing of the past, that on the dissolution of a corporation all its debts were extinguished. There seems to be no valid reason why an ordinary stock corporation, charged with the performance of no public duty, should not be allowed to close up its business at any time and dissolve."[3]

§ 597. **Forfeiture of charter.**[4]—The grant of a corporate privilege or franchise is always subject to the implied condition that it will not be abused.[5] When the corporation has done

[1] Boston, etc., Co. v. Langdon, 24 Pick. (Mass.) 49, Wilgus' Cases; Town v. Bank, 2 Doug. (Mich.) 530. See Mylrea v. Railroad Co. (Wis.), 67 N.W. Rep. 1138. The franchise can not be surrendered by the officers of the corporation. Jones v. Bank of Leadville, 10 Colo. 464. See opinion of counsel, as to the surrender of the Connecticut charter, in 1 Trumbull's Hist. of Conn. 407.

[2] Taylor Priv. Corp., § 434; Merchants' & P. Line v. Wagner, 71 Ala. 581, Wilgus' Cases.

[3] Holmes, etc., Co. v. Holmes, etc., Co., 127 N. Y. 252.

[4] See Wilgus' Cases, The State and the Corporation.

[5] Chicago, etc., Co. v. Needles, 113 U. S. 574. When a corporation violates the provisions of its act of incorporation, or any other law binding upon it, and so misuses its franchise in matters which concern the essence of the

some act or omission which is expressly made a cause of forfeiture, or the violation of the law of its existence is of such a nature as to injuriously affect the public interests, the state will, in a proper proceeding brought for the purpose, deprive the corporation of its charter.[1] But leave will not be granted to institute such a proceeding where the corporation is solvent and carrying out the purposes of its creation, unless there is a clear and willful abuse or non-use of its franchise.[2] As a general rule, in the absence of a legislative statement to the contrary, a forfeiture can be effected only by the judgment of a proper tribunal in proceedings brought by the state to enforce the forfeiture.[3] It does not result *ipso facto* from acts or neglect which will justify the forfeiture.[4] Where a penalty is prescribed for an act it is generally held to be the only punishment intended by the legislature and a forfeiture will not be declared.[5] The state may waive the forfeiture, but only through the action of the legislature.[6] Mere neglect of the officers of a corporation to have its property listed for taxation is not sufficient ground for a forfeiture of its charter.[7]

A deliberate attempt by a corporation to evade an important provision of the insurance law of the state is ground for a forfeiture.[8] The mere non-residence of the officers, directors and stockholders of a domestic corporation is not, in the absence of a statute requiring residence, a ground for the forfeiture of its franchise.[9] But the fact that a corporation has removed its

contract between it and the state, so that it no longer fulfills the purposes for which it was created, the state has an interest in restraining the further exercise of its corporate powers, and may maintain an action for the appointment of a receiver. State v. American, etc., Assn., 64 Minn. 349.

[1] State v. Oberlin, etc., Assn., 35 Ohio St. 258.

[2] State v. Minnesota, etc., Co., 40 Minn. 213; People v. Chicago, etc., Exchange, 170 Ill. 556, 39 L. R. A. 373; People v. N. R., etc., Co., 121 N. Y. 583.

[3] See § 94, *supra*; State v. Janesville, etc., Co., 92 Wis. 496, 32 L. R. A. 391; Spartanburg v. Spartanburg, etc., R. Co., 51 S. C. 129; Leese v. Atchison, etc., R. Co., 24 Neb. 143, 8 Am. St. Rep. 179.

[4] Parker v. Bethel, etc., Co., 96 Tenn. 252, 31 L. R. A. 706.

[5] State v. Real Estate Bank, 5 Ark. 595

[6] Dern v. Salt Lake City R. Co. (Utah), 56 Pac. Rep. 556; People v. Phœnix Bank, 24 Wend. (N. Y.) 431.

[7] North, etc., Co. v. People, 147 Ill. 234, 24 L. R. A. 462.

[8] International Frat. Alliance v. State, 86 Md. 550.

[9] North, etc., Co. v. People, 147 Ill. 234.

principal place of business and all of its agencies out of the state of its creation, in contravention of the public policy of the state as shown by its general system of legislation, is a sufficient ground for forfeiting its charter. A charge against a corporation of falsely and fraudulently posing as a domestic corporation when it has in fact removed to a foreign state is not proven by the fact that the local office is not at all times open and the books there, if the corporate property is within the state and the officers and books are at the office as frequently as required by the business. The mere fact that the books have been kept most of the time in a foreign state contrary to the statute is not a sufficient ground of forfeiture, if the places of location are both near the boundary line and the books have been produced at the general office whenever anyone entitled to see them wished for them.[1] A statute which provides that the secretary and treasurer of every domestic corporation shall reside, have their place of business and keep the books of the corporations within the state is not complied with by the residence within the state of a person who is nominally secretary and treasurer, while the corporate business is transacted in another state.[2] Mere non-user[3] and the sole ownership of all the stock by one person will not cause a dissolution without a judicial decree.[4] An act by a corporation tending to cause injury to the public by affecting the welfare of the people is an abuse of its franchise for which the charter may be forfeited on an information in the nature of quo warranto.[5]

[1] Simmons v. Norfolk, etc., Co., 113 N. C. 147; 22 L. R. A. 677.

[2] State v. Park. & Nelson L. Co., 58 Minn. 330.

[3] That a corporation is not *ipso facto* dissolved by an act of non-user or misuser, which is a cause of forfeiture, see State v. Spartanburg, etc., R. Co. (S. C.), 28 S. E. Rep. 145; State v. Atchison, etc., R. Co., 24 Neb. 143, 8 Am. St. Rep. 164; Atchison, etc., R. Co. v. Nave, 38 Kan. 744, 5 Am. St. Rep. 800. Non-user of one of several privileges is not ground for forfeiture. Wadesboro, etc., Co. v. Burns, 114 N. C. 353. Forfeiture for non-user or otherwise is a question between the state and the corporation, and can not be raised by a private litigant. Petition of Philadelphia, etc., R. Co., 187 Pa. St. 123; Coquard v. National, etc., Co., 171 Ill. 480.

[4] Parker v. Bethel, etc., Co., 96 Tenn. 252.

[5] People v. Chicago, etc., Exch., 170 Ill. 556, 39 L. R. A. 373. The unlawful granting of a diploma by a school of osteopathy, in good faith under legal advice, is not a ground for the forfeiture of its charter. Corpora-

Thus, the charter of a water-works company will be annulled if, instead of furnishing pure wholesome well water, as required by its charter and contract, it, during four droughts in two years, supplies impure river water and refuses for insufficient reasons to sink additional wells. The fact that all water supply will cease if the charter is vacated, and that after suit is commenced the company offers to sink the required wells, will not prevent the decree being entered.[1]

The exercise of franchises and privileges not granted by law may be a serious usurpation and encroachment which when it injures or puts in hazard the rights of any person will justify the forfeiture of its charter.[2] An insurance company may forfeit its charter by deliberately exceeding the amount it is allowed by law to insure on one life.[3] A statute which authorizes an injunction to restrain the exercise of franchises and privileges, or the transaction of unauthorized business by a corporation does not exclude the remedy by proceedings to forfeit the charter.[4] The right of the state to declare the forfeiture of the charter of a water-works company for breach of duty imposed by the charter is not taken away by a provision in a contract between the company and the city that the city may rescind the contract if the company fails to observe its conditions.[5] Long delay in moving for a forfeiture, and active compulsion upon the company by requiring it to extend its operations, is a waiver of the right to forfeit the franchise of a water company for neglecting to keep accurate accounts of the cost of construction as required by the ordinance which authorizes the construction of the works, and provides for the purchase of the

tions are political trustees, and their charters will not be forfeited for either acts of omission or commission done in good faith. State v. National School of Osteopathy, 76 Mo. App. 439.

[1] Capital, etc., Co. v. State, 105 Ala. 406, 29 L. R. A. 743.

[2] Hartnett v. Plumbers' Sup. Assn., 169 Mass. 229, 38 L. R. A. 194.

[3] International Frat. All. v. State, 86 Md. 550, 40 L. R. A. 187.

[4] International Frat. All. v. State, 86 Md. 550, 40 L. R. A. 187. An action may be brought by the attorney-general in the name of the state, under the Wisconsin statutes, to vacate the charter of a street-railway corporation for failure to exercise its franchise. Wright v. Milwaukee, etc., Co., 95 Wis. 29, 36 L. R. A. 47.

[5] Capital City, etc., Co. v. State, 105 Ala. 406, 29 L. R. A. 743.

plant by the city under certain conditions.[1] Findings that a corporation has for a long time failed to complete the work for which it was created; that its members have ceased to have an interest in the management of its business or the completion of its work, and that a judicious sale of its property would greatly advance the work already done will justify an order of dissolution.[2]

§ 598. **Loss of integral part.**[3]—The dissolution of a corporation by the loss of an integral part can very rarely occur in modern times. The rule that a corporation is dissolved by the death of all its members has no application to modern business corporations. Their shares pass by assignment, bequest or descent, and must always be the property of some person who is necessarily a member of the corporation.[4] But if all the members of a non-stock corporation die or withdraw, and there is no method by which their places can be filled, the corporation is dissolved.[5] But it is not dissolved by the failure to elect officers where a method is provided for filling vacancies.[6] The common law rule is thus stated by Chancellor Kent:[7] "A corporation may also be dissolved when an integral part of the corporation is gone, without whose existence the functions of the corporation can not be exercised, and when the corporation has no means of supplying that integral part and has become incapable of action. The incorporation becomes then virtually dead or extinguished."

§ 599. **Statutory method of dissolution by the state.**—Statutes now generally provide methods for the dissolution and

[1] State v. Janesville, etc., Co., 92 Wis. 496.

[2] State v. Cannon River, etc., Assn., 67 Minn. 14. A corporation organized as a savings bank under Minnesota Laws, 1867, chapter 23, which paid its depositors, sold its assets and good-will, and did no business for sixteen years, and then under Laws 1889, chapter 233, changed its name and place of business, and exercised its corporate powers without objection by the state, is at least a *de facto* corporation. Richards v. Minnesota, etc., Bank (Minn.), 77 N. W. Rep. 822.

[3] See Wilgus' Cases.

[4] Boston, etc., Co. v. Langdon, 24 Pick. (Mass.) 49, Wilgus' Cases.

[5] Lehigh, etc., Co. v. Lehigh, etc., Co., 4 Rawle (Pa.) 9; Russell v. McLellan, 14 Pick. (Mass.) 63.

[6] Parker v. Bethel, etc., Co., 96 Tenn. 252.

[7] 2 Kent's Com. (13th ed.), 309. See 1 Rolle Abr. 514.

winding up of corporations. It may be either at the instance of stockholders or of the state. Thus, in Minnesota, an action may be brought by the attorney-general in the name of the state for the purpose of vacating the charter or annulling the existence of a corporation other than municipal, whenever such corporation (1) offends against any of the provisions of the act or acts creating, altering or renewing such corporation; or (2) violates the provisions of any law by which such corporation forfeits its charter by abuse of its powers; or (3) whenever it has forfeited its privileges or franchises by failure to exercise its powers; or (4) whenever it has done or omitted to do any act which amounts to a surrender of its corporate rights, privileges and franchises; or (5) whenever it exercises a franchise or privilege not conferred upon it by law. The statute also provides for vacating or annulling the act of incorporation when it appears that it was obtained through some fraudulent suggestion or concealment of a material fact.[1]

§ 600. **Voluntary liquidation.**—It is a well-settled rule that, in the absence of a statutory provision, the shareholders in a private business corporation can not extinguish its charter or dissolve it, and that a court of equity can not dissolve it at their instance. The majority of the stockholders may discontinue the business, but this will not ordinarily effect a dissolution until followed by a decree of a court of competent jurisdiction.[2] But in some states it is provided that when a majority in number or interest of the members[3] desire to close the business and wind up the corporation, they may apply by a petition to the proper court of the county where the corporation has its principal place of business, setting forth in substance the grounds of their application; and the court, after such notice, as it deems proper to all parties interested, may proceed to hear the matter, and, for reasonable cause, adjudge a dissolution of the corporation. A corporation so dissolved is deemed

[1] See Gen. St. Minn. 1878, ch. 79, §§ 1, 2.

[2] § 602, Treadwell v. Salisbury, etc., Co., 7 Gray (Mass.) 393, 404.

[3] A suit seeking a dissolution may be instituted by stockholders holding not less than one-third interest. See Weigand v. Alliance, etc., Co., 44 W. Va. 133.

and held extinct in all respects as if the charter had expired by its own limitation.

§ 601. **Statutory provisions for a temporary continuance of corporation.**—It is now generally provided by statute that a corporation shall continue for a certain period after its formal dissolution for the purpose of winding up its business.[1] The proceedings under such a statute are governed entirely by the statute.[2] The majority of the stockholders during this period can not sell the corporate property to a new corporation of which they are directors and stockholders, at a valuation determined by themselves, against the will of the minority and compel the minority to accept either stock in the new corporation or pay on the basis of the estimated value of the property. Minority stockholders are entitled to have the property sold.[3] A national bank continues to exist after the expiration of the statutory period of its existence, as a legal person capable of suing and being sued, until its affairs are fully settled.[4]

§ 602. **Insolvency, sale or loss of property—Abandonment of business.**[5]—The legal existence of a corporation is not affected by its insolvency, as the possession of property is not necessary to corporate existence.[6] "If their property is impaired or wholly gone, this seems to be no reason, before such surrender or forfeiture, to prevent the members from furnishing renewed capital and then proceeding to use the corporate power."[7] A corporation is not dissolved by the mere disposal of all of its

[1] For illustrations, see State v. Fogarty, 105 Iowa 32; Miller v. Newburg, etc., Co., 31 W. Va. 836; Am. Surety Co. v. Great, etc., Co. (N. J.), 43 Atl. Rep. 579; Singer v. Talcot, etc., Co., 176 Ill. 48.

[2] As to these statutes, see Hanan v. Sage, 58 Fed. Rep. 651; Life Assn. v. Fassett, 102 Ill. 315; Bowe v. Minn., etc., Co., 44 Minn. 460; Cooper v. Oriental Sav. Assn., 100 Pa. St. 402; Wright v. Nostrand, 94 N. Y. 31; Herring v. N. Y., etc., R. Co., 105 N. Y. 340; Nelson v. Hubbard, 96 Ala. 238; Foster v. Bank, 16 Mass. 245. See Spratt v. Livingston, 32 Fla. 507, 22 L. R. A. 453.

[3] Mason v. Mining Co., 133 U. S. 50.

[4] Farmers' Nat'l Bank v. Backus (Minn.), 77 N. W. Rep. 142.

[5] See Wilgus' Cases.

[6] Moseby v. Burrow, 52 Tex. 396; National Bank v. Insurance Co., 104 U. S. 54.

[7] Coburn v. Boston, etc., Co., 10 Gray (Mass.) 243; Boston, etc., Co. v. Langdon, 24 Pick. (Mass.) 49, Wilgus' Cases; Reichwald v. Hotel Co., 106 Ill. 439; Auburn, etc., Co. v. Sylvester, 68 Hun (N. Y.) 401.

property,[1] or by the fact that one member has acquired all the stock,[2] or that its shares are held by a less number of persons than the law requires for the organization of a corporation,[3] or by the burning of the mill, to operate which the corporation was organized.[4] The sale of all the property may have the effect of terminating the business for which the corporation was organized, but it does not dissolve it.[5] Such a sale no more dissolves the corporation than would the giving of a mortgage that might ultimately result in all the property being taken from the corporation. The corporation still exists, and is properly made a party to an action as an existing corporation. A corporation is not dissolved by an assignment for the benefit of creditors,[6] the appointment of a receiver,[7] or the discontinuance of business.[8]

§ 603. **Powers of a court of equity.**—As a general rule a court of equity has no power, unless it is conferred by statute, to decree the dissolution of a corporation by forfeiture of its franchises, either at the suit of an individual or at the suit of the state, as there is an adequate remedy at law by quo warranto.[9] "General jurisdiction of suits against corporations no

[1] See Louisville, etc., Co. v. Kaufman (Ky.), 48 S. W. Rep. 434; James v. Western, etc., Co., 121 N. C. 523; Weigand v. Alliance, etc., Co., 44 W. Va. 133.

[2] Louisville, etc., Co.v. Eisenman, 94 Ky. 83, Wilgus' Cases. It remains a corporation aggregate, but the franchise is suspended until the shares are transferred, when corporation may continue its business in the corporate name. Button v. Hoffman, 61 Wis. 20. But see Swift v. Smith, etc., Co., 65 Md. 428.

[3] Parker v. Bethel, etc., Co., 96 Tenn. 252.

[4] In re Belton, 47 La. Ann. 1614, 30 L. R. A. 648.

[5] Price v. Holcomb, 89 Iowa 123, 56 N. W. Rep. 407; Bump v. Butler Co., 93 Fed. Rep. 290. As to power of the majority to sell all the property of the corporation, see Bartholomew v. Derby Rubber Co., 69 Conn. 521, 61 Am. St. Rep. 57, and note; Benbow v. Cook, 115 N. C. 324, 44 Am. St. Rep. 457. §485, *supra*.

[6] Town v. Bank, 2 Doug. (Mich.) 530; State v. Butler, 86 Tenn. 614.

[7] Kincaid v. Dwinelle, 59 N. Y. 548; State v. District Court (Mont.), 56 Pac. Rep. 219; Moseby v. Burrow, 52 Tex. 396.

[8] Saline National Bank v. Prescott (Kan.), 57 Pac. Rep. 12; Brandt v. Benedict, 17 N. Y. 93; Slee v. Bloom, 5 Johns. Ch. (N. Y.) 366, 19 Johns. (N. Y.) 456.

[9] Republican, etc., Co. v. Brown, 58 Fed. Rep. 644, 19 U. S. App. 203, 24 L. R. A. 776; Wallace v. Pierce-Wallace, etc., Co., 101 Iowa 313, 38 L. R. A. 122; Folger v. Columbian, etc., Co., 99 Mass. 267; Strong v. McCagg, 55

more implies a power to destroy a corporation at the suit of an individual than jurisdiction of private suits against individuals authorizes the court to entertain a prosecution for crime, to pass sentence of death, and to issue a warrant for execution. The only modes of dissolving a corporation known to the common law were, by the death of all its members, by act of the legislature, by a surrender of the charter, accepted by the government, or by forfeiture of the franchise, which could only take effect upon a judgment of a competent tribunal on a proceeding in behalf of the state; and neither a court of law nor a court of equity had jurisdiction to decree a forfeiture of the charter or dissolution of the corporation at the suit of an individual."[1] "Equity may properly," says Mr. High, "compel officers of corporations to account for any breach of trust in their official capacity; yet in the absence of statutes extending its jurisdiction, it will usually decline to assume control over the management of the affairs of a corporation upon a bill * * * alleging fraud, mismanagement and collusion on the part of the corporate authorities, since such interference would necessarily result in the dissolution of the corporation, and the court would thus accomplish indirectly what it has no power to do directly. The remedial power exercised by courts of equity in such cases ordinarily extends no further than the granting of an injunction against any special misconduct on the part of the corporate officers; and although the facts shown may be sufficient foundation for such an injunction, the court will not enlarge its jurisdiction by taking the affairs of the corporation out of the management of its own officers and placing them in the hands of a receiver."[2] But a court of

Wis. 624; Bliven v. Peru, etc., Co., 9 Abb. N. Cas. 205; Mason v. Supreme Court, 77 Md. 483; Oakes v. Hill, 14 Pick. 442; Hunt v. Le Grand, etc., Co., 143 Ill. 118; Supreme Sitting, etc., v. Baker, 134 Ind. 293. For the English rule see In re Lloyd Generale Italiano, L. R. 29 Ch. Div. 219; Hardon v. Newton, 14 Blatchf. 376; Hodges v. Screw Co., 3 R. I. 9; Denike v. Cement Co., 80 N. Y. 599; Hitch v. Hawley, 132 N. Y. 212.

[1] Folger v. Columbian, etc., Co., 99 Mass. 267; Boston, etc., Co. v. Langden, 24 Pick. 49. See Texas, etc., Co. v. Starrow, 92 Fed. Rep. 5.

[2] High on Receivers, § 238. See Republican Mountain Silver Mines v. Brown, 7 C. C. A. 412, 58 Fed. Rep. 644, and cases there cited. A court of

equity may, in order to give complete relief from frauds practiced through a corporate organization, and, if necessary, will, dissolve the corporation.[1]

§ 604. **Proceedings by state.**—No one can take advantage of a breach of the conditions on which a corporation was granted its franchises for the purpose of depriving it of such franchises but the state by which it was created,[2] unless authorized to do so by statute.[3] A number of persons who were members of the defendant corporation obtained a rule requiring the corporation to show cause why an information in the nature of a quo warranto should not be filed against it, for the purpose of dissolving it and procuring an adjudication that its corporate powers were void. The statute under which the corporation had been formed "required the holders of stock to pay fifty per cent. of their subscriptions within sixty days after the first meeting of the company, and that no insurance on any one risk should be made for a larger sum than ten per cent. of the capital stock actually paid in." The complainants

one state may appoint a receiver for a corporation organized in another state, and doing business within its own territory and having property there. This may be done although the courts in the home state of the corporation may have placed its affairs in the hands of a receiver. The receiver appointed in the foreign state will be regarded as ancillary or auxiliary to the receiver appointed in the state to which the corporation owes its creation. See Holbrook v. Ford, 153 Ill. 633, 27 L. R. A. 324; Hunt v. Columbian, etc., Co., 55 Maine 290, 92 Am. Dec. 592; Lewis v. American Sav. and Loan Assn., 98 Wis. 203; In re Matheson Brothers, Limited, L. R. 27 Ch. Div. 225. Although a court has jurisdiction to appoint an ancillary receiver to take control of the assets of a foreign corporation within its jurisdiction, it should be exercised only when there is reason to believe that the assets will not be properly handled by the general receiver. See In re Jarvis, etc., Co., 11 Law Times Rep. 373.

[1] Miner v. Belle Isle Ice Co., 93 Mich. 97, Wilgus' Cases.

[2] Elizabethtown, etc., Co. v. Green, 46 N. J. Eq. 118; State v. Curtis, 35 Conn. 374, Wilgus' Cases; Heard v. Talbot, 7 Gray (Mass.) 113; Toledo, etc., R. Co. v. Johnson, 49 Mich. 148; Greenbrier, etc., Co. v. Ward, 30 W. Va. 43; Renick v. Bank, 13 Ohio Rep. 298; Boston, etc., Co. v. Langdon, 24 Pick. 49, Wilgus' Cases. The fact that a suit by the attorney-general to annul the existence of a corporation as an illegal combination to regulate the price of a commodity was instituted on the petition of another such corporation is immaterial. People v. Milk Exchange, 145 N. Y. 267, 27 L. R. A. 437.

[3] State v. Webb, 97 Ala. 111, Wilgus' Cases.

alleged that the defendant corporation had violated both provisions of the statute. Chief Justice Parsons said:[1] "We have not inquired into the truth of these allegations, as we are satisfied that in this case such inquiry would be immaterial, because this rule is not moved for in behalf of the commonwealth. * * * An information for the purpose of dissolving the corporation or of seizing its franchises can not be prosecuted but by the authority of the commonwealth. * * * For the commonwealth may waive any breaches of any condition, expressed or implied, on which the corporation was created; and we can not give judgment for the seizure by the commonwealth of the franchises of any corporation, unless the commonwealth be a party in interest to the suit, and thus assenting to the judgment." The proceeding is now generally regulated by statute. At common law the proceeding to enforce a forfeiture of corporate franchises might be by *scire facias*, or by quo warranto. The former was used when there was a legal corporation which was abusing its powers, and the latter when there was no legal incorporation and a mere assumption of power.[2]

§ 605. **Effect of dissolution, generally.**—Upon the dissolution of a corporation it is dead, and loses all power to act, and its affairs must be wound up by an officer appointed for the purpose. Thereafter it can neither institute nor defend a suit,[3] and a judgment entered against it is a nullity.[4] All pending suits

[1] Commonwealth v. Union, etc., Co., 5 Mass. 230.

[2] 2 Kent. Com., 313; Wheeler v. Pullman, etc., Co., 143 Ill. 197.

[3] Saltmarsh v. Planters, etc., Bank, 17 Ala. 761; Muscatine, etc., v. Funck, 18 Iowa 469; City Ins. Co. v. Bank, 68 Ill. 348; Boston, etc., Co. v. Langdon, 24 Pick. 49, Wilgus' Cases. In Decree v. Hankinson (C. C. A.), 92 Fed. Rep. 49, reversing 84 Fed. Rep. 876, it was held that the dissolution of a corporation by the forfeiture of its charter does not deprive it of the power to convey its property or to maintain or defend suits relating to the settlement of its business.

[4] Marion, etc., Co. v. Perry, 74 Fed. Rep. 425, 41 U. S. App. 14, 33 L. R. A. 252; Thornton v. Marginal, etc., R. Co., 123 Mass. 32; Dobson v. Simonton, 86 N. C. 492; Krutz v. Town Co., 20 Kan. 397. *Scire facias* to review a judgment recovered as a corporation can not be maintained after its dissolution. Mumma v. Potomac Co., 8 Pet. (U. S.) 281. Can not be proceeded against unless specially authorized by statute. Combes v. Keyes, 89 Wis. 297, 27 L. R. A. 369.

are abated,[1] but the dissolution of a defendant corporation after an action on contract has been submitted and taken under advisement by the court will not abate the action, as the court will date the findings and enter judgment as of the time when the action was submitted.[2] The forfeiture of the charter will not prevent the sale of its property under a levy of an execution made before the dissolution.[3] A statute making void a judgment confessed by a corporation after a petition has been filed for its dissolution will not affect the control of the property attached according to the laws of another state under the judgment.[4]

§ 606. **Effect of dissolution upon corporate debts and assets.** —The property and property-rights of a corporation are not under the present law destroyed by the expiration of the corporate charter.[5] By the common law rule, upon the dissolution of a corporation its real estate reverted to the grantor, its personal property went to the sovereign, and its debts were extinguished.[6] "According to the old settled law of the land," says Chancellor Kent,[7] "where there is no special statute provision to the contrary, upon the civil death of a corporation all of its real estate remaining unsold reverts back to the original grantor and his heirs. The debts to and from the corporation are all extinguished. Neither the stockholders nor the directors or trustees of the corporation can recover those debts or be charged with them in their natural capacity. All the

[1] Nat'l Bank v. Colby, 21 Wall. (U. S.) 609; McCulloch v. Norwood, 58 N. Y. 562; Thornton v. Marginal, etc., R. Co., 123 Mass. 32. Effect of consolidation, Evans v. Interstate, etc., R. Co., 106 Mo. 594.

[2] Shakman v. U. S., etc., Co., 92 Wis. 366, 32 L. R. A. 383. In Steinhouer v. Colmar (Colo. App.), 55 Pac. Rep. 291, it was held, under Gen. St., § 270, that a judgment could be entered after dissolution if the cause of action arose before the dissolution.

[3] Boyd v. Hankinson (C. C. A.), 92 Fed. Rep. 49. This is without reference to the matter of a preference.

[4] Com. Nat'l Bank v. Motherwell, etc., Co., 95 Tenn. 172, 29 L. R. A. 164.

[5] People v. O'Brien, 111 N. Y. 1, 7 Am. St. Rep. 684, and note; Fleitas v. New Orleans (La.), 24 So. Rep. 623.

[6] Angell & Ames Corp., § 779; Life Assn. v. Fassett, 102 Ill. 315; Commercial Bank v. Lockwood, 2 Harr. (Del.) 8.

[7] Kent Com. (13 ed.), 307; 11 Kyd. Corp., 516; Co. Litt. 13*b*.

personal estate of the corporation vests in the people as succeeding to this right and prerogative of the crown at common law." But this rule is no longer applicable to business corporations, and the courts of equity will see that the assets of a corporation are collected and applied to the payment of its debts and any surplus distributed among stockholders.[1] It still applies, however, upon the dissolution of a corporation which has no stockholders and no debts, such as a mutual insurance company, and to religious and charitable corporations.[2] Thus, upon the dissolution of the corporation known as the Church of Jesus Christ of Latter Day Saints, it was held that the property of the corporation escheated to the United States. The court said,[3] that "when a business corporation instituted for the purposes of gain or private interest is dissolved, the modern doctrine is, that its property after the payment of its debts equitably belongs to its stockholders. But this doctrine has never been extended to public or charitable corporations. As to these the ancient established rule remains, namely, that when a corporation is dissolved, its personal property, like that of a man dying without heirs, ceases to be the subject of private ownership, and becomes subject to the disposal of the sovereign authority; whilst its real estate reverts or escheats to the grantor or donor, unless some other course of devolution has been directed by positive law, though still subject, as we shall hereafter see, to the charitable use." The property of the corporation devolved upon the United States, subject to be disposed of according to the principles applicable to property devoted to religious and charitable uses, the real estate being also subject to a condition of forfeiture and escheat contained in the act of congress.

[1] Wheeler v. Pullman, etc., Co., 143 Ill. 197; Heman v. Britton, 88 Mo. 549; Asheville Div. v. Aston, 92 N. C. 578; Hightower v. Thornton, 8 Ga. 486; Wilson v. Leary, 120 N. Car. 90, 58 Am. St. Rep. 778.

[2] Titcomb v. Insurance Co., 79 Maine 315. As to the property of an incorporated military company, which has been disbanded by order of the governor for non-compliance with the law, see Cummings v. Hollis (Ga.), 33 S. E. Rep. 919.

[3] Late Corp. of Church of Jesus Christ v. United States, 136 U. S. 1, Wilgus' Cases.

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