PSEUDO-FOREIGN CORPORATIONS

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RECENTLY there has been an attempt at legislation specially subjecting "pseudo-foreign corporations" to certain provisions of local corporation law.¹ This event invites a re-examination of the whole question of the application of local law to corporations essentially local in character but incorporated in a foreign state. Momentarily ignoring the criteria for determining when the foreign corporation is essentially local in character, let us assume the clearest case of localness: a business conducted entirely or predominantly within the state by local residents. The prototype of the pseudo-foreign corporation can well be the local hotel owned entirely by local residents but incorporated out of state—say, in Delaware. The belief seems to prevail that the local corporation law, aside from the part devoted expressly to foreign corporations and treating mostly problems of admission and jurisdiction, has no application to foreign corporations, however pseudo-foreign they may be. According to this view, it is absurdly easy to avoid any uncongenial feature of local corporation law; one can simply incorporate in a state where there is no such feature, and, according to reputable authority, "it is no fraud or evasion of the laws of a state for its citizens intending to act only in their own state to form themselves into a corporation under the laws of another state."² Can it be that the law is really so simple, and so blind?

It is submitted that the dogmatic treatment of all corporations chartered in other states as foreign corporations exempt from local law neither should be nor actually is the rule in practice. That a distinction should be made between pseudo-foreign and truly foreign corporations will appear from an examination of the possible theoretical justifications for treating the two alike. It is hoped that this examination will also lay bare some of the underlying policy considerations to be served by any rule dealing with the problem of foreign corporations. Then the actual judicial decisions will be examined, and it will be shown that although these decisions seem superficially to support the conclusion that pseudo-foreign corporations are beyond the reach of local law,

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1. The General Statutes Commission of North Carolina submitted to the 1955 General Assembly a proposed New Business Corporation Act. S. Bill No. 49, 1955 Sess. The Bill defined "pseudo-foreign corporation" and made certain provisions of the local corporation law applicable to such a corporation. The Bill was enacted, to become effective July 1, 1957, but the provisions relating to "pseudo-foreign" corporations were eliminated. N.C. Sess. Laws 1955, c. 1371.

2. 2 BEALE, CONFLICT OF LAWS 775 (1935).

they do not in reality go so far. They are, in fact, reconcilable with an approach that makes a distinction between pseudo-foreign corporations and the genuinely foreign variety, even though that distinction has not yet been expressly delineated in the decisions themselves. Then, having seen that distinctive treatment of pseudo-foreign corporations should be the rule, and could be so far as case precedent is concerned, we shall look into the constitutional aspects of the proposed rule, and finally examine the way that other countries have dealt with the problem. First, let us explore the possible policy bases of the traditional view, which is that a pseudo-foreign corporation is no different from any other foreign corporation, and so must be governed by the law of the state of its incorporation.

THE THEORETICAL JUSTIFICATIONS FOR GOVERNING A PSEUDO-FOREIGN CORPORATION BY THE LAW OF THE CHARTERING STATE

1. *The Charter as a Contract*

One possible explanation for exempting pseudo-foreign corporations from local law might be the view that a corporate charter is a contract, so that ordinary conflicts choice-of-law rules for contracts must apply. Then the validity of the contract is determined by the law of the place of execution (which is, let us assume without argument, the incorporating state). Or the validity and effect of the contract may be governed by the law of any reasonably related state selected by the parties, the state of incorporation being one such reasonably related place, even if the only reason the contract was executed there was to seek the coverage of its law and the exclusion of other law.

This explanation will not do. Aside from the theoretical difficulty of governing "outsiders" (e.g., creditors) by the charter contract, there is much more to a corporation than a mere contract. There is no point in rehashing the "franchise" or "grant" or "privilege" aspects of the corporate charter, nor in discussing the nature of the legal personality of the entity that arises from incorporation. Suffice it to say that the corporate charter, though a contract, is one that is *sui generis*, especially as relates to freedom of contract. This charter freedom has never been left unbounded: specific provisions are often required or forbidden, by courts as well as by legislatures.³ Legislation relating to corporations not infrequently contains protective provisions that the parties to be protected cannot "waive" by contract in drafting the charter. For example, a court would surely not uphold a charter clause to the effect that no shareholders can inspect those books and records that the law otherwise entitles them to inspect.⁴ It is not logical that local law be automatically excluded simply because parties have, by selecting the place of incorporation, exercised

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3. Indeed, freedom of contract has been denied, under corporation laws as interpreted by the courts, where the parties involved were merely seeking reasonable business arrangements. See *Benintendi v. Kenton Hotel, Inc.*, 294 N.Y. 112, 60 N.E.2d 829 (1945); *Kaplan v. Block*, 183 Va. 327, 31 S.E.2d 893 (1944).

4. See *State ex rel. Cochran v. Penn-Beaver Oil Co.*, 34 Del. 81, 143 Atl. 257 (1926).

freedom of contract on a matter that local law does not leave completely to freedom of contract. And finally, even if one were to view the corporate charter as a "mere contract," it is by no means clear that under the principles of conflict of laws strong local public policy could be evaded by making the contract in another state for the very purpose of circumventing local law.⁵

2. *The Corporation as the "Creature" of the Chartering State*

It might be argued that the out-of-reach view is an inescapable consequence of the doctrine that the corporate person is created by the foreign state, and that only the creator can give the entity the structure and the organs by which it operates; it alone can prescribe the functioning, duties and responsibilities of the organism and its parts.

True enough, corporation law has had a flair for getting entangled in legal mysticism, probably because of the metaphysical vistas opened by the concepts of corporation and personality. But we have had enough troubles in corporation law with reasoning based on the concept of corporations as creatures of the sovereign⁶ without pushing this highly nonfunctional dogma into new territory. Anyway, the argument proves too much in the light of existing law: witness the application (by statute) of the former California rule of shareholders' super-added liability even to other states' corporate creatures doing business in California and there incurring debts.⁷ Furthermore, the "creation" dogma can be met with an argument of the same breed: it is equally plausible to maintain that in the case of the pseudo-foreign corporation the creature's structure and organs are transformed by the power of the new superimposed local sovereign, so as to take on some of the same functions, duties and responsibilities of local creatures. Obviously this quasi-theology gets us nowhere.

3. *Certainty and Ease of Application*

The exclusive supremacy of the law of the state of incorporation may be suggested as the only rule of certainty and easy application. It cannot be

5. *Personal Finance Co. v. Gilinsky Fruit Co.*, 127 Neb. 450, 256 N.W. 511 (1934) (loan and assignment of local wages made out-of-state); *London Finance Co. v. Shattuck*, 221 N.Y. 702, 117 N.E. 1075 (1917) (local lender had loan applications sent out of state for acceptance). See also *King v. Bruce*, 145 Tex. 647, 201 S.W.2d 803 (1947) (elaborate out-of-state transaction to change community property into separate property). In all these cases, the out-of-state evasive scheme did not work.

6. One recalls the difficulties persisting to this day in suits against foreign corporations from the doctrines and fictions that were developed to circumvent the dicta of Chief Justice Taney in *Bank of Augusta v. Earle*, 38 U.S. (13 Pet.) 519 (1839), to the effect that a corporation cannot exist outside the state of its creation, that a corporation cannot migrate. *Id.* at 586-90. See HENDERSON, *THE POSITION OF FOREIGN CORPORATIONS IN AMERICAN CONSTITUTIONAL LAW* cc. 3, 5 (1918). Similarly, viewing a corporation as a "creature of the law" has contributed to the difficulties of the ultra vires doctrine. See *Central Transp. Co. v. Pullman's Palace Car Co.*, 139 U.S. 24 (1891). Perhaps judicial conservatism in failing to "disregard the corporate entity" can also be partly attributed to the creation theory.

7. *Thomas v. Matthiessen*, 232 U.S. 221 (1914); *Penney v. Nelson*, 183 U.S. 144 (1901). See *RESTATEMENT, CONFLICT OF LAWS* § 191 (1934).

denied that the rule has these qualities—nor that any other rule runs into difficulties of interpretation and application. Take, for example, a possible alternative rule: that the governing law of a pseudo-foreign corporation should be the local corporation law. Obviously not all of that law would be intended to apply—not, for instance, the purely procedural formalities of incorporating.⁸ But if not all of the local law, then what parts? Even if the question is not insoluble, it runs into the familiar difficulties that arise when a juridical line is to be drawn. Likewise, there is the thorny problem of determining when a corporation is pseudo-foreign. None of these troubles is presented by the traditional view. Even more clearly than in the case of an individual, we know with certainty where the corporate creature was born and who created it.⁹

Even admitting that certainty and ease of application are highly desirable features in legal principles, however, there remains the question how big a price we want to pay for certainty when a rule giving us certainty leads to undesirable results. We have had the same problem with the doctrine that a corporation is a “separate entity” from its stockholders. The doctrine is easy, certain—almost beautiful; but literally applied, it gives results that are sometimes ludicrously unrealistic. And so an antidote has been worked out: the separate entity will be disregarded when necessary to avoid an undesirable result.¹⁰ Thus if a corporation is too “thinly” capitalized the enterpriser may find that he has lost his limited liability or at least his pretended creditor status.¹¹ This is clearly a departure from certainty and a venture into determining how thin is too thin. The sensible solution in dealing with the separate entity, and with the pseudo-foreign corporation as well, is to stick to the certain rule until—but only until—there are strong policy reasons for doing otherwise.

4. *The Difficulty of Matching Local Law to Foreign Charters*

Is choice of the incorporating state's law dictated, even in the case of the pseudo-foreign corporation, by the impossibility of applying local law to a structure whose gears won't mesh with local law? One can think of awkward situations arising if local corporation law were applied to a foreign corporation. For example, if the local statute were construed to mean that in a certain class of shares entitled to vote on a particular matter each share shall be entitled to one vote (or to not more than one vote),¹² its application to a foreign corporation's balanced voting scheme (e.g., with voting rights geared to the amounts of capital contributions) might be most disturbing. Again, if local laws provide

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8. Cf. *Demarest v. Flack*, 128 N.Y. 205, 28 N.E. 645 (1891).

9. This isn't true in the case of the multiple-incorporated enterprise. See Foley, *Multiple Incorporation and the Conflict of Laws*, 42 HARV. L. REV. 516 (1929).

10. BALLANTINE, CORPORATIONS 292-93 (rev. ed. 1946); STEVENS, CORPORATIONS 85-95 (2d ed. 1949).

11. BALLANTINE, CORPORATIONS 302-03 (rev. ed. 1946); LATTY, SUBSIDIARIES AND AFFILIATED CORPORATIONS cc. 5, 6 (1936); STEVENS, CORPORATIONS 85-95 (2d ed. 1949).

12. Query whether the MODEL BUSINESS CORPORATION ACT § 31 (1953 Draft) is susceptible of this interpretation.

that the initial by-laws must be adopted by the first board of directors, whereas in the state of incorporation by-laws are adopted by the subscribers (shareholders) before election of the first board of directors, one might be somewhat uncertain about how to apply the local law.

The argument proves no more than that if local law were to be applied it would have to be applied on a selective basis. The selection might well be limited to those protective features of local law that indicate a fairly strong policy of safeguarding the particular local interests in question (creditors, stockholders). If local law, for example, imposes liability on directors of local corporations for paying dividends when the resulting ratio of assets to liabilities is reduced below three-to-two,¹³ the application of that feature of local law to a pseudo-foreign corporation would protect local interests with which the local state is legitimately concerned. It could be imposed without technical difficulty as an additional restriction on dividends beyond those imposed by the state of incorporation. One could go that far with the pseudo-foreign corporation without having to contend that a *real* foreign corporation is, absent express local statutes, subject to dividend restrictions other than those imposed by the law of the chartering state. A fortiori, such a choice-of-law principle would not subject nationally operating corporations—"cosmopolites"—to the varying dividend laws of the many states in which they operate.¹⁴

5. *Outright Conflict Between Local and Foreign Law*

Similar to the point just discussed is the argument that adherence to the incorporating state's law is justified as an effort to avoid the possibility of an impasse when the courts of the local state make a requirement directly opposed to one made by the other state. In such a case management wouldn't know what to do. Suppose that there are 100,000 common shares and 40,000 preferred shares entitled to vote on a recapitalization by charter amendment, and 55,000 of common and 18,000 of preferred voted for the amendment. Suppose further that in the incorporating state a majority of all the shares, bunched as a unit, can adopt the amendment, whereas in the local state it would take a majority of each class. It is conceivable that after the amendment became duly effective by the law of the state of incorporation the court of the local state might order the corporation to treat the shares as unchanged, while the court of the other state would decree exactly the opposite.

It is doubtful, however, that this possibility of conflict justifies complete exclusion of local law despite the local character of the enterprise. For one thing, the matter is not left entirely to the rival mercies of the two state courts; the United States Supreme Court has the role of determining which court, or which law, must give way. Furthermore, unless the two state laws are totally incompatible, such deadlocks are matters within the insiders' control, since by appropriate charter clauses even corporations in the less exacting juris-

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13. See, e.g., N.C. GEN. STAT. § 55-116 (1950).

14. For rationalizing the choice of the incorporating state's law in such a case, see Coleman, *Corporate Dividends and the Conflict of Laws*, 63 HARV. L. REV. 433 (1950).

dictions can usually adopt higher requirements. And in matters where a clear local policy of a protective nature can be discerned, the charter sponsors might well be required, if they want to avoid the impasse, to draft their charter accordingly. The only burden this would create would be that of studying the statutes of both states before resorting to a pseudo-foreign corporation.

6. *Antiquated Local Laws*

The traditional view might be supported by a policy of allowing a corporation to choose to operate under an up-to-date body of corporate law—one that is complete, and technically abreast of legitimate business needs and modern financing techniques—where the local law is obsolete. But it is one thing to permit a corporation to avoid archaic provisions of local law¹⁵ (which would probably not express a vigorous public policy in any event), and quite another to allow it to avoid a strong local policy, of which only the local courts and legislature should be the judges. And at any rate this argument should not appeal to a court of, say, California or Ohio, both of which states make a constant effort to improve their corporation laws and keep them geared to legitimate business needs. The most plausible reason for Californians or Ohioans organizing a Delaware corporation to do a predominantly California or Ohio business is, presumably, simply to evade the local corporation law.

7. *Lack of a Local Policy*

The rule of immunity of foreign corporations from local regulation as repeated by some state courts may be traceable to a view that the local corporation laws do not really embody any provisions of firm public policy that might not just as well be supplanted by the corresponding provision of the foreign law. True, many corporation statutes have become largely enabling rather than regulatory acts. That is, they go to great length and detail in clarifying the operation of the various corporate organs and in spelling out exactly how to go about effecting all those varied transactions in which a corporation may find itself, without seriously curtailing the corporation's freedom of action in the interest of community welfare.¹⁶ Conceivably, then, a court in a state having a mere enabling

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15. Until recently, good examples of such archaic provisions were to be found in the corporation laws of the District of Columbia and Texas.

16. Of course no corporation act can really avoid making some "regulatory" choices, no matter how much of a mere "enabling act" the draftsman was striving for. One never sees, for instance, a statutory dividend provision that reads, "Dividends shall be payable from such sources, irrespective of the financial condition of the corporation, as the charter may provide," or a comparable provision for other returns of corporate property to shareholders. A completely logical theory of free bargaining would urge that such a provision would be perfectly sound, since creditors, before extending credit, can always look to see how protective or unprotective to creditors is the charter of this particular corporation. Even the favorite incorporation states embody a minimum of protection to creditors and shareholders: Delaware, for instance, forbids loans to officers and directors, gives even non-voting shares a vote on fundamental matters, and requires a class vote on some of these matters.

act for its corporation law might see little point to holding pseudo-foreign corporations to any local rule. But such an attitude would not be justified under a local corporation law that contains carefully worked out protective features.

8. *Local Policy Improper*

Finally, someone may urge that local legislatures have no business seeking to safeguard particular interests (creditors, shareholders in general, minority shareholders or particular classes of shareholders) by protective provisions that go beyond the minimal protection afforded by other states. The argument collapses of its own weight, and yet it would seem to be the only possible explanation of judicial decisions that would hold that provisions carefully inserted in the local corporation law with a serious protective purpose can, no matter how purely local is the enterprise, be evaded by the simple device of foreign incorporation.

There is, in sum, no cogent reason why vigorous community policies expressed in particular portions of a modern corporation law should not outweigh considerations of mere certainty and ease of application. There is no justification for immunizing an essentially local corporation from such policy-laden local law simply because the corporation was chartered in another state. It remains to be seen whether the law is as it clearly should be.

CASES APPARENTLY EXCLUDING LOCAL LAW

Turning from discussion of theory and policy to an examination of the cases, one finds that the hegemony of the law of the chartering state over a pseudo-foreign corporation is by no means as clear as a hurried reading would indicate. The cases that seem at first glance to look to the law of the state of incorporation as the exclusive governing law can be grouped into three categories in terms of the specific issues dealt with: (1) the cases where the question was whether the local court could take jurisdiction of a suit involving the "internal affairs" of a corporation chartered in a foreign state; (2) those presenting the broad issue of valid corporate existence; and (3) those turning on the specific question whether the incorporating state's law should apply.

Jurisdiction of the Local Court over a Foreign Corporation

There are a group of cases that purport to follow the doctrine that except where there is fraud, or possibly mismanagement, a local court will not interfere with the "internal affairs" of foreign corporations,¹⁷ and will not exercise "visitorial power" (whatever that means)¹⁸ over such corporations. These

17. 17 FLETCHER, CYCLOPEDIA PRIVATE CORPORATIONS § 8425 (perm. ed. 1933); RESTATEMENT, CONFLICT OF LAWS §§ 196-97, 199 (1934).

18. On the emptiness of that resounding phrase "visitorial power" or "visitatorial power," see *State ex rel. Weede v. Iowa So. Util. Co.*, 231 Iowa 784, 813-16, 2 N.W.2d 372, 388-90 (1942).

cases have been a fertile source of statements that, by the cumulative effect of sheer repetition, have given foreign corporations an aura of immunity to local laws relating to the internal affairs of corporations.

If the internal affairs doctrine were really strictly followed¹⁹ it would be a standing invitation to circumvent all provisions in the local corporation law that regulate internal matters (which would include most matters touching the interests of stockholders and creditors), however strong the policy behind the provisions might be. Then the only courts that could take jurisdiction of an internal affairs case would be those of the state of creation; and those courts, we can safely assume, would apply their own law governing the particular internal affair without regard to the law of the state with which the corporation is wholly identified in reality, unless and until the United States Supreme Court were to require them to do otherwise. For example, if by the corporation's charter and the law of the state of creation voting for directors is "straight," whereas the local state has a strong statutory policy favoring cumulative voting, then the locally operating pseudo-foreign corporation could, by the internal affairs doctrine, escape the local law: the local court would not look into the challenged election, and the court of the state of creation would, presumably, count the ballots "straight."

Actually, the internal affairs doctrine should be viewed as a mere misnomer for *forum non conveniens*.²⁰ If frankly recognized as a problem of balance of convenience, and not a slot-machine matter, the question whether the local court should hear cases involving even internal matters would seem to be an easy one where the corporation in question is pseudo-foreign. Be that as it may, one finds that even working within the formula of the internal affairs doctrine, courts make a sharp distinction when it comes to corporations whose business and personnel are predominantly identified with the local state, as shown by such factors as the places where the business is done, the location of property and records, and the location of the residence and meetings of directors.²¹ Courts have little difficulty in entertaining internal affairs suits in such cases, even to the extent of removing the wrongdoing officers of a pseudo-foreign corporation,²² or appointing receivers, liquidating or otherwise.²³ If in most of these

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19. For a critical appraisal of the internal affairs doctrine, see Notes, 46 COLUM. L. REV. 413 (1946), 33 *id.* at 492 (1933), 97 U. PA. L. REV. 666 (1949). See also *State ex rel. Weede v. Iowa So. Util. Co.*, *supra* note 18.

20. See *Williams v. Green Bay & W. Ry.*, 326 U.S. 549 (1946); *State ex rel. Weede v. Iowa So. Util. Co.*, 231 Iowa 784, 818-27, 2 N.W.2d 372, 391-95 (1942); Notes cited note 19 *supra*.

21. See cases cited in 17 FLETCHER, *op. cit. supra* note 17, § 8427, and in *State ex rel. Weede v. Iowa So. Util. Co.*, *supra* note 20. See also RESTATEMENT, CONFLICT OF LAWS § 197 (1937).

22. *State ex rel. Wurdeman v. Reynolds*, 275 Mo. 113, 204 S.W. 1093 (1918). The court distinguished a prior case on the ground that it had not involved such a completely local enterprise.

23. *Aston v. O'Carroll*, 66 F. Supp. 585 (M.D. Pa. 1946); *Potter v. Victor Page Motors Corp.*, 300 Fed. 885 (D. Conn. 1924); *Scholl v. Allen*, 237 Ky. 716, 36 S.W.2d

cases the local courts nevertheless applied the law of the state of creation, at least they had hurdled the barrier of jurisdiction. Perhaps their actual choice of law was correct in terms of the principles we will discuss shortly.

Validity of Corporate Existence

There are a group of cases wherein one litigant urged that the validity or existence of the foreign corporation should be denied on the ground that the enterprise was entirely local in every aspect and was incorporated in another state simply to take advantage of the corporation law of that state. The courts have almost invariably denied the contention,²⁴ generally in unnecessarily broad language suggesting that pseudo-foreign incorporation will be recognized for all purposes.

The leading case is *Demarest v. Flack*,²⁵ where a group of New Yorkers, having formed a West Virginia corporation²⁶ to own and operate an amusement park in New York City, were personally sued in New York by a customer who was injured while using the corporation's facilities. Recovery was denied. The validity and existence of the foreign corporation must be "recognized," said the court, in an opinion which on the surface seems to give approval to resort to pseudo-foreign corporations:

"If in any particular case it is thought by those interested in the matter that the business can be done in our own state and by our own citizens with greater facility under the form of a foreign corporation than under that of a

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353 (1931); *Starr v. Bankers Union*, 81 Neb. 377, 116 N.W. 61 (1908); *Hogeland v. Tec-Crafts, Inc.*, 39 Pa. County Ct. 10 (Del. C.P. 1951).

A fortiori local courts will appoint a custodial receiver. *Scattergood v. American Pipe & Constr. Co.*, 249 Fed. 23 (3d Cir. 1918); *Fudickar v. Louisiana Loan & Inv. Co.*, 13 F.2d 920 (W.D. La. 1926); *Hill v. Dealers Credit Corp.*, 102 N.J. Eq. 310, 140 Atl. 569 (Ch. 1928).

24. An early New Jersey case disregarded the corporate entity and treated the shareholders of the foreign corporation as partners where the court believed that the corporation should have been chartered under local law for the local business it was conducting. *Hill v. Beach*, 12 N.J. Eq. 31 (Ch. 1858). Coming from a New Jersey court, the following excerpt from the opinion is today not without humor:

"[T]he Belleville Quarry Company [incorporated in New York to own and operate a quarry in New Jersey] cannot be recognized by any court in New Jersey as a legally constituted corporation. If it can, what need is there of any general or special law in our state? Individuals . . . may go into the city of New York, organize under the general laws of that state, erect all manufacturing establishments here, and . . . transact their business, not only free from all personal responsibility, but under cover of a corporation not amenable to our laws. . . . These individuals, then, must be treated and dealt with by the law as partners. . . ."

Id. at 35-36.

25. 128 N.Y. 205, 28 N.E. 645 (1891).

26. In the period 1884-1901, West Virginia apparently was a favorite incorporating state. 2 COOK, STOCK AND STOCKHOLDERS § 935 (3d ed. 1894); CONYNGTON & BENNETT, CORPORATION PROCEDURE 712 (rev. ed. 1927). The reasons were low rates and simple requirements. In 1901, that state raised and complicated the fees and taxes, from an "ill-judged avarice," whereupon it lost its incorporating business. *Ibid.*

domestic one, there is no public policy which forbids the transaction under such form."²⁷

To repeat, *on the surface* these words seem to approve of the institution of the pseudo-foreign corporation. *Actually, no feature of New York law protective of the plaintiff's class was shown to be evaded.* There was, so far as appears, nothing in New York law that would have assured corporate creditors of a more solvent corporation or of a remedy against anyone but the corporation, even if the enterprise had been incorporated under New York law. The court itself made the point: "The freedom from personal liability would be as great, and could as easily be attained, under our own as under the laws of West Virginia," and so there was "really nothing to evade by incorporating under a foreign law,"²⁸ at least insofar as the plaintiff was concerned. If by resorting to a West Virginia corporation the enterprisers circumvented New York taxes and fees, that is no concern of creditors (indeed, this plaintiff may be all the better off for it!). On the other hand, if New York legislation had revealed a policy of holding shareholders in New York corporations liable without limit to tort claimants suffering personal injuries from corporate operations within the state, the result might have been different.²⁹ The case stands only for the proposition that the penalty for that evasion of local corporation law is not denial of limited liability of the shareholders. It does not hold that a pseudo-foreign corporation is an effective evasion device against any and all features of local corporation law.

Demarest v. Flack is typical of the many cases that "recognize" the foreign corporation with words of approval comforting to the pseudo-foreign corporation. In those cases, as in *Demarest v. Flack*, the actual decisions were perfectly sound inasmuch as no local policy was frustrated by the recognition of a foreign charter. A sampling of such cases would include those holding that such a foreign corporation has capacity to sue in the local state³⁰ (whether to enforce a subscription to its stock,³¹ to enforce other contracts³² or to protect its property or other interests);³³ can convey good title to local lands;³⁴

27. *Demarest v. Flack*, 128 N.Y. 205, 217, 28 N.E. 645, 649 (1891). The earlier New York case of *Merrick v. Van Santvoord*, 34 N.Y. 208 (1866), recognized the validity of the Connecticut charter of a locally operating corporation, but the incorporators (not shown to be mere dummies) were Connecticut citizens.

28. *Demarest v. Flack*, 128 N.Y. 205, 216, 28 N.E. 645, 648 (1891).

29. True, it has been held that N.Y. STOCK CORP. LAW § 71, making shareholders liable for debts due to laborers, servants or employees of the corporation, does not apply to foreign corporations. *Armstrong v. Dyer*, 268 N.Y. 671, 198 N.E. 551 (1935); *Gonzalez v. Tuttmann*, 59 F. Supp. 858 (S.D.N.Y. 1945) (collecting citations). *Contra*, *Greenberg v. Rosenwasser*, 147 Misc. 757, 264 N.Y. Supp. 529 (1st Dep't 1933). But it is not at all clear that these cases involved an out-and-out pseudo-foreign corporation.

30. *Troy & N.C. Gold Mining Co. v. Snow Lumber Co.*, 173 N.C. 593, 92 S.E. 494 (1917).

31. *Philadelphia & Gulf S.S. Co. v. Soeffing*, 59 Pa. Super. 429 (1915).

32. *Oakdale Mfg. Co. v. Garst*, 18 R.I. 484, 28 Atl. 973 (1894).

33. *Cumberland Tel. & Tel. Co. v. Louisville Home Tel. Co.*, 114 Ky. 892, 72 S.W. 4 (1903).

34. *Lancaster v. Amsterdam Improvement Co.*, 140 N.Y. 576, 35 N.E. 964 (1894).

can by mandamus force the appropriate local state official to grant it a permit to do business locally even if the corporation's stock structure or organizational steps are not such as would be appropriate for a local corporation³⁵ (even if it was incorporated out of state by local citizens and is seeking admission into the state in the face of a local statute that forbids the admission of foreign corporations formed for "*the purpose of evading our laws*")³⁶; is entitled to exercise and retain its public utility franchise, despite the contention that the corporation was formed in another state solely to do business in this state;³⁷ and does not subject its shareholders to the unlimited personal liability of partners.³⁸

In all the foregoing cases "recognizing" the foreign corporation one finds no words of disapproval of pseudo-foreign corporations.³⁹ But those cases merely hold that such corporations are not "nullities," and are not "prevented from acting" in the local state.⁴⁰ Such holdings would not compel a local court to

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35. *Commonwealth Acceptance Corp. v. Jordan*, 198 Cal. 618, 246 Pac. 796 (1926); *North Am. Petroleum Co. v. Hopkins*, 105 Kan. 161, 181 Pac. 625 (1919); *State ex rel. Standard Tank Car Co. v. Sullivan*, 282 Mo. 261, 221 S.W. 728 (1920); *State ex rel. Fiberboard Products, Inc. v. Hinkle*, 147 Wash. 10, 264 Pac. 1010 (1928) (foreign corporation with different classes of common stock—a scheme not contemplated by local law). It does not appear whether these foreign corporations were pseudo-foreign or simply cosmopolites. For the issue there involved, it should not matter. In the California case the court recognized that the question of equality of voting power among the shares, then required in California corporations, was not involved in this action of mandamus for admittance to do business as a foreign corporation. *Commonwealth Acceptance Corp. v. Jordan*, *supra* at 630, 246 Pac. at 801. The Kansas and Missouri cases involved admittance of corporations having no-par shares into states that had not yet got around to passing no-par statutes. Expressions in some of the opinions in the foregoing cases to the effect that stock structure is a matter of "internal affairs," and that the local court will not look into the internal affairs of a foreign corporation, are to be understood in the light of what the court was actually deciding; *i.e.*, to let the corporation in. Nothing more was involved.

36. *State ex rel. Brown Contracting & Bldg. Co. v. Cook*, 181 Mo. 596, 603, 80 S.W. 929, 930 (1904). As the court apparently construed the statute, the laws of Missouri were not being avoided unless the foreign corporation was formed *for a purpose* not authorized by Missouri law.

37. *State ex rel. Godard v. Topeka Water Co.*, 61 Kan. 547, 60 Pac. 337 (1900). The court construed the charter to authorize this New Jersey corporation to do business *also in New Jersey*, thus avoiding the doctrine of *Land Grant Ry. & T. Co. v. Coffey County*, 6 Kan. 245 (1870), to the effect that a corporation whose charter does not authorize it to operate at home will not, on any principle of comity, be recognized in another state, and hence cannot there maintain suit.

38. *Beal v. Childress*, 92 Kan. 109, 139 Pac. 1198 (1914); *Merrick v. Van Santvoord*, 34 N.Y. 208 (1866). *Contra*, *Hill v. Beach*, 12 N.J. Eq. 31 (Ch. 1858), discussed in note 24 *supra*.

39. "Indeed, the practice, whether good or evil, of taking out charters in one state with which to do business solely in others is too general and has been too long recognized to be now questioned." *Troy & N.C. Gold Mining Co. v. Snow Lumber Co.*, 173 N.C. 593, 594, 92 S.E. 494, 495 (1917).

40. 2 BEALE, CONFLICT OF LAWS 775 (1935). It is significant that Beale's statement that it is no fraud or evasion of the law to incorporate elsewhere, see text at note 2 *supra*, was directed at this question of nullity resulting from such incorporation.

refuse to apply the local statute concerning, say, cumulative voting, to a pseudo-foreign corporation.

Application of a Specific Rule of the Incorporating State

The cases are many where local courts have applied a specific rule of the chartering state to a foreign corporation, with either an implicit assumption or an explicit generalization to the effect that of course that law is to be applied. The cases extend over a vast range of topics, among them liability for allegedly illegal dividends;⁴¹ liability of shareholders for further payments;⁴² the validity of a stock option plan;⁴³ election or appointment of officers;⁴⁴ legality of loans to officers;⁴⁵ validity of a corporation's contract to repurchase its shares;⁴⁶ corporation's lien on shares for shareholder's debt;⁴⁷ validity and revocability of a pre-incorporation subscription to shares;⁴⁸ validity of transfer of shares;⁴⁹ validity of a voting trust;⁵⁰ suit by a dissolved corporation in the absence of statute authorizing such suit;⁵¹ and ability of a dissolved corporation to assign contracts.⁵² Again, as in that group of cases recognizing the "validity" of a pseudo-foreign corporation, the courts frequently talk broadly of the governing law of the state of incorporation. For example, in one of the cases relating to the validity of an agreement to appoint officers, arguably

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41. *National Lock Co. v. Hogland*, 101 F.2d 576 (7th Cir. 1938); *Rockwood v. Foshay*, 66 F.2d 625 (8th Cir. 1933); *Abercrombie v. United Light and Power Co.*, 7 F. Supp. 530 (D. Md. 1934); *Stratton v. Anderson*, 278 Mich. 499, 270 N.W. 764 (1936); *Garetson Lumber Co. v. Hinson*, 69 Ore. 605, 140 Pac. 633 (1914); *Morris v. Sampsel*, 224 Wis. 560, 272 N.W. 53 (1937); cf. *Hamilton v. United Laundries Corp.*, 111 N.J. Eq. 78, 161 Atl. 347 (Ch. 1932). See *Coleman*, *supra* note 14. Occasionally local law is applied without discussion: *Smalley v. Bernstein*, 165 La. 1, 115 So. 347 (1927); *Loan Soc'y v. Eavenson*, 248 Pa. 407, 94 Atl. 121 (1915).

42. *Converse v. Hamilton*, 224 U.S. 243 (1912) (assessment). See also *Broderick v. Rosner*, 294 U.S. 629 (1935); cf. *Cochrane v. Morris*, 10 N.J. Misc. 82, 157 Atl. 652 (Sup. Ct. 1931); *Southworth v. Morgan*, 205 N.Y. 293, 98 N.E. 490 (1912).

43. See *Rogers v. Guaranty Trust Co.*, 288 U.S. 123, 133-50 (1933) (dissenting opinion of Justice Stone). This was the only opinion on the merits. The majority opinion held that it was proper to dismiss the complaint on the basis of the internal affairs doctrine.

44. Cf. *San Remo Copper Mining Co. v. Moneuse*, 149 App. Div. 26, 133 N.Y. Supp. 509 (1st Dep't 1912).

45. *National Lock Co. v. Hogland*, 101 F.2d 576 (7th Cir. 1938). But cf. *Bigelow v. Old Dominion Copper Mining & Smelting Co.*, 74 N.J. Eq. 457, 71 Atl. 153 (Ch. 1908) (local law applied as to liability of promoters for secret profits).

46. *Tolman v. New Mexico & Dakota Mica Co.*, 4 Dak. 4, 22 N.W. 505 (1885); *Peterson v. New England Furniture & Carpet Co.*, 210 Minn. 449, 299 N.W. 208 (1941).

47. *Bishop v. Globe Co.*, 135 Mass. 132 (1883).

48. *Collins v. Morgan Grain Co.*, 16 F.2d 253 (9th Cir. 1926).

49. *Hunt v. Drug, Inc.*, 35 Del. 332, 156 Atl. 384 (1931).

50. *Ringling v. Ringling Bros.-Barnum & Bailey Combined Shows, Inc.*, 29 Del. Ch. 318, 49 A.2d 603 (Ch. 1946), *modified on rehearing*, 29 Del. Ch. 610, 53 A.2d 441 (Sup. Ct. 1947).

51. *Fidelity Metals Corp. v. Risley*, 77 Cal. App. 2d 377, 175 P.2d 592 (1946).

52. *Kratky v. Andrews*, 224 Minn. 386, 28 N.W.2d 624 (1947).

invalid by local law, the court observed that "the plaintiff is a West Virginia corporation, and controlled so far as its internal management is concerned by the statutes of that state."⁵³

These cases do not, however, establish an inescapable doctrine that the local court must apply the foreign corporation law without taking into account such factors as the essentially local character of the enterprise, the predominance of local residents among the interests protected by a particular feature of local corporation law, or the vigor of the policy supporting that feature. The actual decisions are reconcilable with an analysis that weighs such factors against the traditional rule's certainty and ease of application. The cases that appear to enunciate the rigid rule of looking to the law of incorporation can, I believe, be seen to fall into one or more of the following categories:

1. The foreign corporation in question may not have been doing all or even the major part of its business locally. In other words, the court was simply announcing a general rule applicable to real foreign corporations, not pseudo-foreign ones.⁵⁴

2. There was no need to apply local corporation law in view of the absence of those interests with whose protection local law legitimately has a high concern.⁵⁵ For example, no matter how otherwise localized a foreign corporation or its business may be, if a majority of the shares are held by non-residents there is no point to applying the local corporation law that all shareholders are entitled to vote,⁵⁶ at least in the absence of a showing that citizens of the local state are bearing the brunt of the voting discrimination permitted under an out-of-state charter. There is no particular reason in such a case for the local state to make the voting rights its business.

3. No showing was made that there was any basic difference between the laws of the two states.⁵⁷

4. The application of the law of the state of incorporation would not run counter to any strong policy of local corporation law.⁵⁸ This would certainly

53. *San Remo Copper Mining Co. v. Moneuse*, 149 App. Div. 26, 28, 133 N.Y. Supp. 509, 511 (1st Dep't 1912).

54. Many of the cases cited in notes 41-52 *supra* may well have been of this kind, but the reports do not reveal the fact. One knows, for example, that the American Tobacco Company, an out-of-state corporation involved in litigation over a stock option plan in the federal courts in New York in *Rogers v. Guaranty Trust Co.*, 288 U.S. 133 (1933), can by no stretch of imagination be said to be so essentially a New York corporation that in that jurisdiction it must be viewed as pseudo-foreign.

55. Compare *Stark Bros. Nurseries & Orchards Co. v. Little*, 257 Fed. 421 (7th Cir. 1919) (Montana filing requirement with penalty of directors' liability to creditors for its violation held inapplicable to a foreign corporation; creditor-plaintiff a Missouri concern) with *Nelson v. Bank of Fergus County*, 157 Fed. 161 (8th Cir. 1907) (same Montana statute applicable to a foreign corporation; local creditor involved).

56. *Allen v. Montana Refining Co.*, 71 Mont. 105, 227 Pac. 582 (1924).

57. See, e.g., *Stratton v. Anderson*, 278 Mich. 499, 270 N.W. 764 (1936); *Hamilton v. United Laundries Corp.*, 111 N.J. Eq. 78, 161 Atl. 347 (Ch. 1932); *Garetson Lumber Co. v. Hinson*, 69 Ore. 605, 140 Pac. 633 (1914).

58. See *Groesbeck v. Beaupre*, 307 Ill. App. 215, 30 N.E.2d 531 (1940) (suit to en-

be the case where the foreign state's protective measures are more stringent than the local ones. For example, it is hard to show that any local policy, much less a strong one, is violated by application of the law of the state of incorporation that forbids loans by a corporation to its officers,⁵⁹ or that forbids a corporation to buy its own shares.⁶⁰ True, the local state may permit local corporations to engage in such transactions, but not for vital policy reasons.

5. Application of any law other than that of the state of incorporation would, in view of the particular facts of the case, be impracticable⁶¹ or inequitable.⁶²

All of these holdings may be summarized by saying that the courts looked first to the law of the state of incorporation and, finding no particular local policies substantial enough to overbalance the convenience of applying the foreign law, applied it.

CASES APPLYING LOCAL LAW

Not all the cases treat pseudo-foreign corporations as truly foreign, of course: there are a formidable number of cases applying local law to such corporations. But just as the decisions we have just been discussing tend to be couched in misleading, overgeneralized terms, the decisions choosing local law, even though they are generally sound, use a variety of verbal formulae equally generalized and uninformative.

There are a group of cases turning on the question of the "situs" of an essentially localized corporation, allowing local garnishment of shares held by a defendant in such a corporation⁶³ or of a debt owed by such a corporation.⁶⁴ One encounters in such cases judicial expressions that the corporation in question "was born, it is true, in New Jersey, but it lives, moves and has its being in this state";⁶⁵ or is only "nominally a corporation of the other

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force superadded liability of shareholder); *Edwards v. Schillinger*, 245 Ill. 231, 91 N.E. 1048 (1910) (local enforcement of stock subscription fictitiously paid up by means of a dividend when the corporation was insolvent); *Young v. Farwell*, 139 Ill. 326, 28 N.E. 845 (1891) (local enforcement of superadded shareholders' liability under law of state of incorporation refused, out of further deference to that law); *Peterson v. New England Furniture & Carpet Co.*, 210 Minn. 449, 299 N.W. 208 (1941) (shareholder's suit to compel corporation to purchase his share, contrary to a charter provision which apparently would have been equally lawful by local corporation law).

59. *National Lock Co. v. Hogland*, 101 F.2d 576 (7th Cir. 1938).

60. *Tolman v. New Mexico & Dakota Mica Co.*, 4 Dak. 4, 22 N.W. 505 (1885).

61. *Converse v. Hamilton*, 224 U.S. 243 (1912) (suit by receiver to enforce liability of shareholders under the law of the state incorporation).

62. *Young v. Farwell*, 139 Ill. 326, 28 N.E. 845 (1891). This suit by a creditor to enforce liability of local shareholders under local law was dismissed because the courts of the incorporating state had not determined the extent of liability for corporate debts of shareholders in that state.

63. *Wait v. Kern River Mining & Development Co.*, 157 Cal. 16, 106 Pac. 98 (1909); *Young v. South Tredegar Iron Co.*, 85 Tenn. 189, 2 S.W. 202 (1886).

64. *Goodwin v. Claytor*, 137 N.C. 176, 49 S.E. 173 (1904).

65. *Id.* at 183, 49 S.E. at 176.

state";⁶⁶ or that "its residence . . . anywhere else outside of California is the merest fiction."⁶⁷ Relying on such cases, a New York court did not even mention New Jersey in passing upon the legality of the removal of an officer of a corporation chartered in New Jersey but predominantly identified with New York.⁶⁸

Another series of cases find the law of the chartering state inapplicable on the ground that it is contrary to local public policy—although for the most part they involve a public policy of a now outmoded sort. For example, at a time when local policy did not grant the incorporation privilege readily but instead required a special act of the legislature, thus subjecting the proposed financing to an initial screening, a New Jersey court held that this policy could not be evaded by forming a New York corporation under the New York general incorporation law to own and operate a quarry in New Jersey.⁶⁹ Likewise, at a time when local legislative policy did not extend the limited liability corporate privilege to an enterprise conducting a general merchandising business, the formation of an out-of-state corporation to operate a purely local business of that type was viewed as a "fraud upon the law" of both the incorporating state and the local state, and the associates were held personally liable as partners.⁷⁰ The legislative background of this case is now archaic, but the decision itself is not eccentric if viewed as holding not that an evasive pseudo-foreign corporation should be "disregarded," but rather that certain features of local law are so important that a local court will apply them at least to the pseudo-foreign corporation.

Similarly, if local corporation law throws around the limited liability achieved by incorporation certain safeguards for the protection of creditors, the local courts may refuse to see those safeguards evaded by the pseudo-foreign corporation device, at least if the judiciary sets high store by the safeguards. At one time, for example, Missouri, like many other states, required that all of the authorized capital stock be subscribed and that half of it be paid in before the corporation could be organized.⁷¹ When a group of Missouri residents

66. *Ibid.*

67. *Wait v. Kern River Mining & Development Co.*, 157 Cal. 16, 21, 106 Pac. 98, 100 (1909).

68. *McQuade v. Stoneham*, 230 App. Div. 57, 242 N.Y. Supp. 548 (1st Dep't 1930), *rev'd on other grounds*, 263 N.Y. 323, 189 N.E. 234 (1934) (the "New York Giants" baseball enterprise).

69. *Hill v. Beach*, 12 N.J. Eq. 31 (Ch. 1858). On a bill for an accounting, the corporate entity was ignored and the shareholders were viewed as partners. Although it does not appear that the interested associates were New Jersey citizens, the court apparently believed that an enterprise such as this required a local charter, even though it might have viewed otherwise a New York corporation formed to carry on an essentially New York business but whose activities spilled over into New Jersey.

70. *Empire Mills v. Alston Grocery Co.*, 15 S.W. 200, *on rehearing*, 15 S.W. 505 (Tex. Ct. App. 1891).

71. In European law to this day such a feature of corporation law is apparently considered an essential safeguard against irresponsible ventures. The new Spanish corporation law requires full subscription of all shares and one-fourth payment before the corporation can be formed. Law of July 17, 1951, (*Ley de Régimen Jurídico de las Sociedades Anóni-*

seeking to finance and operate an exposition in St. Joseph, Missouri, formed a Colorado corporation with an authorized capital stock of \$1,000,000, of which only \$43,000 was ever paid in, the local court protected the corporation's creditors by holding the incorporators to unlimited personal liability.⁷² The result is sound, even if the court's reasoning that no principle of comity required the court to recognize the corporation as such proves too much. That is, the result is sound so long as the Missouri subscription and payment provisions are thought to reflect a strong protective policy.

A more modern variety of protective legislation, concerning the shareholder's right to inspect corporate books, was involved in the case of *Toklan Royalty Corp. v. Tiffany*.⁷³ Here the Oklahoma court faced the question whether to apply to a Delaware-chartered corporation the Delaware statute on the shareholder's right to inspect corporate books, which required the shareholder to allege and prove his "proper" motive, or the Oklahoma statute, which had no such requirement. The court chose the Oklahoma law—principally, one suspects, because of the pseudo-foreign character of the corporation. This corporation, said the court, referring with approval to the terms "migratory" and "tramp" corporations, "is not, strictly speaking, a foreign corporation with respect to the question of examination and inspection of its books and records by its stockholders."⁷⁴ The court bolstered its opinion by reference to an "equal treatment" provision for foreign corporations in the Oklahoma Constitution⁷⁵ and by an overstated argument that the word "corporation" in local corporation laws is meant, unless the contrary appears, to include foreign corporations.⁷⁶

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mas), art. 8, BOLETIN OFICIAL Aug. 6, 1951. French law makes the same requirement. Law of July 24, 1867, arts. 1, 24 (under CODE DE COMMERCE, art. 64). Italian law is similar: CODICE CIVILE art. 2329 (1942). So is German law: Law of Jan. 30, 1937 (*Aktiengesetz*) § 28(2), [1937] REICHSGESETZBLATT I.107. See 1 MANUAL OF GERMAN LAW 240 (England 1950).

72. *Cleaton v. Emery*, 49 Mo. App. 345 (K.C. Ct. App. 1892). It should be noted that this case is not necessarily inconsistent with *State ex rel. Brown Contracting & Bldg. Co. v. Cook*, 181 Mo. 596, 80 S.W. 929 (1904), which allowed a pseudo-foreign corporation to be admitted into the state even though it was allegedly formed to evade local law. See note 36 *supra*. In fact, although it made a feeble attempt to distinguish the *Cleaton* case on the ground of noncompliance with Colorado law (to which the *de facto* doctrine would seem to be a sufficient answer), the court in the later case seemed to approve of the *Cleaton* decision.

The *Cleaton* case antedated the 1903 Missouri statute which recited that foreign corporations formed to evade Missouri law would, if admitted to do business in Missouri, subject the shareholders to partnership liability. Mo. Laws of 1903, pp. 121, 122-23. The *Cook* decision was *after* passage of the statute, but still sidestepped it. See note 36 *supra* and accompanying text.

73. 193 Okla. 120, 141 P.2d 571 (1943).

74. *Id.* at 122, 141 P.2d at 573. It does not appear from the report, however, that the shares of this "foreign" corporation were held predominantly or substantially by local residents.

75. "No foreign corporation . . . shall be relieved from compliance with any of the requirements made of a similar domestic corporation. . . ." OKLA. CONST. art. IX, § 44.

76. A similar willingness to look into the "internal affairs" (corporate elections)

Sometimes the local courts will not bother to question the foreignness of a corporation, but simply indulge in an expansive construction of the local substantive law in order to apply it to essentially localized foreign corporations.⁷⁷ For instance, there is a New York statute making directors of foreign corporations doing business in New York liable under the provisions of the New York Stock Corporation law, like directors of New York corporations, if they do certain enumerated acts.⁷⁸ The statute might have been construed to mean that any liability of directors of foreign corporations imposed by the *state of incorporation* would be *enforced* in New York.⁷⁹ But the court of appeals construed it to subject the directors of a New Jersey corporation to the substantive liability imposed by New York law;⁸⁰ and the corporation in question subsequently recovered from a director the amount of unlawful dividends paid

and to apply the provisions of local corporation statutes (prescribing the procedure for judicial inquiry into an election) was displayed by an Idaho court dealing with an Arizona corporation all of whose properties were in Idaho. *Hunter v. Merger Mines Corp.*, 67 Idaho 115, 170 P.2d 800 (1946). The court noted that the corporation's "sole operation, for [the] purpose of working the property, is in Idaho," *id.* at 119, 170 P.2d at 801, but again an "equal treatment" statute served as a make-weight: "Foreign corporations . . . shall be subject to the laws of the state applicable to like domestic corporations." IDAHO CODE ANN. § 30-510 (1948).

77. For example, when faced with a foreign corporation whose principal place of business was in Montana, a court held that the Montana statute imposing liability on directors for failure to make certain annual filings was meant to apply to foreign corporations. *Nelson v. Bank of Fergus County*, 157 Fed. 161 (8th Cir. 1907). The plaintiff here was a local creditor. But the same statute was held not so to apply in *Stark Bros. Nurseries & Orchards Co. v. Little*, 257 Fed. 421 (7th Cir. 1919). In the latter case it was only reported that the foreign corporation was "doing business" locally, but it is generally known that the Stark nursery enterprise is essentially not a Montana enterprise. Incidentally, the plaintiff was not in this case a local creditor.

78. N.Y. STOCK CORP. LAW § 114, reads as follows:

"Except as otherwise provided in this chapter, the officers, directors, and stockholders of a foreign stock corporation transacting business in this state, except a moneyed or a railroad corporation, shall be liable under the provisions of this chapter, in the same manner and to the same extent as the officers, directors, and stockholders of a domestic corporation, for the making of

1. Unauthorized dividends;
2. Unlawful loans to stockholders;
3. False certificates, reports or public notices;
4. Illegal transfers of the stock and property of such corporations, when it is insolvent or its insolvency is threatened.

"Such liabilities may be enforced in the courts of this state, in the same manner as similar liabilities imposed by law upon the officers, directors and stockholders of domestic corporations."

For the legislative history of the above-quoted statute, see *Irving Trust Co. v. Maryland Cas. Co.*, 83 F.2d 168 (2d Cir. 1936); KEHL, *CORPORATE DIVIDENDS* 307-08 (1941).

79. See *German-American Coffee Co. v. Diehl*, 167 App. Div. 928, 152 N.Y. Supp. 1113 (1st Dep't 1915), where the court below had sustained a demurrer to the complaint against the directors on this interpretation and on the square authority of *De Raismes v. United States Lithograph Co.*, 161 App. Div. 781, 146 N.Y. Supp. 813 (1st Dep't 1914).

80. *German-American Coffee Co. v. Diehl*, 216 N.Y. 57, 109 N.E. 875 (1915), *reversing* 167 App. Div. 928, 152 N.Y. Supp. 1113 (1st Dep't 1915).

during his term, even though under New Jersey law the cause of action did not run to the corporation.⁸¹ Whether or not the court was influenced by the predominantly local flavor of the particular corporation it was dealing with,⁸² in construing the statute it quite definitely had in mind the pseudo-foreign corporation.⁸³

Again, one notes that some of the local statutes that are expressly made applicable to foreign corporations in matters of what may be called internal affairs seem to be invoked in full force only against predominantly localized enterprises. Thus an Iowa statute that made applicable to foreign public utility corporations certain sections of local Iowa corporation law relating to the amount and kind of consideration required to be received upon the issuance of shares,⁸⁴ was applied to a Delaware corporation with utility properties solely in Iowa, in *State ex rel. Weede v. Iowa Southern Utilities Co.*⁸⁵ Even though the corporation had certain attributes of the cosmopolite, in that much of its financing apparently came from outside the state and some of its directors' meetings were held in New York City and Chicago,⁸⁶ the court emphasized its essentially local character—perhaps not too difficult to establish in a business with clearly localized land, plant and equipment and which locally produces a product all (or substantially all) of which is sold locally.⁸⁷ It should

81. See *German-American Coffee Co. v. O'Neil*, 102 Misc. 165, 169 N.Y. Supp. 421 (Sup. Ct. 1918).

Under New Jersey law, unless the corporation is insolvent, the liability runs to the *stockholders*, not to the corporation. N.J. STAT. ANN. § 14:8-19 (1939), *Fleisher v. West Jersey Securities Co.*, 84 N.J. Eq. 55, 92 Atl. 575 (Ch. 1914).

82. As to this, insufficient facts are reported. The opinion states that the corporation maintained its main business office in New York, there held all the regular and "most" of the special meetings of the board of directors, and there "managed, directed and conducted its business." *German-American Coffee Co. v. Diehl*, 216 N.Y. 57, 60, 109 N.E. 875 (1915). The corporation may have been only in low degree pseudo-foreign—it may have been one of the many cosmopolite corporations with executive headquarters in New York. The doctrine of the case seems later to have been applied to the latter type of corporation. *Irving Trust Co. v. Maryland Cas. Co.*, 83 F.2d 168 (2d Cir. 1936).

83. "In these days, when countless corporations, organized on paper in neighboring states, live and move and have their being in New York, a sound public policy demands that our Legislature be invested with this measure of control." Cardozo, J., in *German-American Coffee Co. v. Diehl*, *supra* note 82, at 64, 109 N.E. at 877.

84. IOWA CODE ANN. § 495.1 (1949). The statute was probably enacted in the belief that overvaluation of securities has an influence on rate regulation.

85. 231 Iowa 784, 2 N.W.2d 372, *supplemental opinion*, 4 N.W.2d 869 (1942) (on demurrer to complaint); *State ex rel. Weede v. Bechtel*, 239 Iowa 1298, 31 N.W.2d 853 (1948), *cert. denied*, 337 U.S. 918 (1949) (same case, on the merits).

86. These facts appear in later litigation involving some of the same parties. See *Des Moines Bank & Trust Co. v. George M. Bechtel & Co.*, 243 Iowa 1007, 51 N.W.2d 174 (1952).

87. "While it was, and is, in law a legal resident of Delaware, and has its technical domicile there, its 'commercial' or 'economic' domicile is in Iowa. It was conceived in Iowa, born in Delaware, and has lived its entire life in Iowa. . . . Its existence in Delaware is an illusory mirage, more atmospheric than real. Under the circumstances, it is, in actuality, more domestic than foreign." Bliss, C.J., in *State ex rel. Weede v. Iowa So. Util. Co.*, 231 Iowa 784, 807, 2 N.W.2d 372, 386 (1942).

be noted that the *Iowa Southern Utilities* case involved the very "internal" question whether new stock issued in exchange for old under a recapitalization plan should be cancelled.⁸⁸ The court applied Iowa law to test the validity of the shares, and was thus enabled to apply its own standard of *fairness* to the plan, instead of the Delaware standard with its unconcern about fairness.⁸⁹ It may be that the occasion has never presented itself, but the fact remains that the Iowa statute in question has never been applied to a foreign public utility corporation whose main business is out of state.

The *Iowa Southern Utilities* case involved a statute specifically aimed at foreign corporations, but it suggests the question whether a foreign-chartered enterprise may be so thoroughly local that a rearrangement of shareholders' rights in the enterprise is a matter of local concern, so that a court will apply protective features of local law even *without* the aid of a statute making local law applicable to the foreign corporation. For example, Nebraska in 1951 passed a statute⁹⁰ aimed at one of the most criticized aspects of modern corporations—unfair recapitalization plans that manage nevertheless to corral the necessary votes. This statute requires the plan to do more than present a vote score card; the plan, if challenged, must be fair and equitable, to a court's satisfaction. Obviously, some strongly felt policy led to this legislation. Now, suppose that Nebraskans incorporate their Omaha department store in Delaware and sell the shares, preferred and common, to local residents. On petition by one of these preferred shareholders to enjoin a preferred-stripping recapitalization, it is quite likely that the Nebraska court would require the plan to measure up to Nebraska standards of fairness. We need not inquire whether the hypothetical corporation was formed in Delaware for the very purpose of evading this particular Nebraska law: it should make no difference, although if that fact were shown the court could be expected to mention it to make the decision look more incontrovertible. Indeed, such a decision might be more logical than was the application of the local statute in *Iowa Southern Utilities*—where, for all that appears, the prejudiced class of shareholders may have consisted largely of non-residents.

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88. The precise issue was whether the new common stock received under a recapitalization plan by the insider who engineered the plan and who owned nearly all the old common stock, should be cancelled. Under the recapitalization plan the several pre-existing valuable classes of preferred stock and the wholly *worthless* (as the court viewed it) common stock all were eliminated by charter amendment and were replaced by a single class of common stock, of which the old worthless common got over half a million dollars' worth. *State ex rel. Weede v. Iowa So. Util. Co.*, 231 Iowa 784, 2 N.W.2d 372 (1942).

89. As to the Delaware attitude toward a "fairness" requirement, see *Barrett v. Denver Tramway Corp.*, 53 F. Supp. 198, 203-05 (D. Del. 1944). Under Delaware law all that is necessary to effectuate such a recapitalization is to follow the Delaware statute and to muster the required votes, except for "fraud" and the rare case where "vested rights" are impaired. See *Keller v. Wilson & Co.*, 21 Del. Ch. 391, 190 Atl. 115 (Sup. Ct. 1936).

90. NEB. REV. STAT. § 21-1,162 (Supp. 1953).

STATUTES BEARING ON APPLICATION OF LOCAL LAW TO PSEUDO-FOREIGN CORPORATIONS

On that most sensible of distinctions—differentiating between the real foreign corporation and the out-and-out pseudo-foreign corporation—the state statutes have been completely silent. Neither the many constitutional or statutory provisions that explicitly or inferentially make local corporation law applicable to all foreign corporations nor those ostensibly immunizing all foreign corporations from local statutes offer any substantial guidance to the courts in drawing that common-sense line.

"Equal Treatment" Statutes

There are constitutional provisions or statutes in more than half of our states approximating locally active foreign corporations to local ones. Although the state provisions vary, they can be roughly classified. The largest category comprises those constitutional provisions or statutes that say, in one way or another, that foreign corporations admitted to do business locally are not to get better local treatment than domestic corporations. The commonest provisions state that foreign corporations are admitted to do local business on "no more favorable conditions" than domestic corporations;⁹¹ or are to do business subject to the same regulations, limitations and liabilities (or privileges or powers);⁹² or shall exercise "no greater" privileges, powers, franchises, etc.⁹³ In addition, scattered provisions are found subjecting foreign corporations doing local business "to all the provisions of the laws of this state",⁹⁴ or to "the provisions of this title [the corporation law], so far as the

91. ARIZ. CONST. art. XIV, § 5; CAL. CONST. art. XII, § 15; KY. CONST. § 202; UTAH CONST. art. XII, § 6.

92. ARK. CONST. art. XII, § 11; MICH. STAT. ANN. c. 195, § 21.98 (Supp. 1953); MINN. STAT. ANN. § 303.09 (West 1946); MISS. CODE ANN. § 5341 (1942) (and "shall . . . become to all intents and purposes a corporation of this state"); N.D. REV. CODE § 10-1712 (1943) (and "shall be subject to the laws of this state"); S.D. CODE § 11.2101 (1939) (corporations, as well as officers and agents, are subject to "all the liabilities and restrictions" imposed on domestic corporations of like character); TENN. CODE ANN. § 4127 (Williams 1934); W. VA. CODE ANN. § 3091 (1949).

93. ARK. CONST. art. XII, § 11; D.C. CODE ANN. § 29-933a (Supp. 1951); FLA. STAT. ANN. § 613.02 (Supp. 1954); HAWAII REV. LAWS c. 157, § 8392 (1945); IDAHO CONST. art. XI, § 10; ILL. ANN. STAT. c. 32, § 157-103 (Smith-Hurd 1954); IND. ANN. STAT. § 25-302 (Burns 1948) ("to the same extent as if it had been organized under this act . . ."); KAN. GEN. STAT. § 17-505 (1949); MO. ANN. STAT. § 351-575 (Vernon 1952); MONT. CONST. art. XV, § 11; MONT. REV. CODES ANN. § 15-1709 (1947); N.M. STAT. ANN. § 51-10-1 (1953); OKLA. CONST. art. IX, § 44 (foreign corporation not to be "relieved from compliance with any of the requirements made of a similar domestic corporation"); OKLA. STAT. ANN. tit. 18, § 1.199 (1953); ORE. REV. STAT. § 57-660 (1953); VA. CONST. art. XII, § 163 (not "relieved from compliance with any of the requirements made of a similar domestic corporation," if no resulting discrimination against the foreign corporation); WIS. STAT. § 180.807 (1953).

94. MD. ANN. CODE GEN. LAWS art. 23, § 85 (1952). Similar language is found in a number of the provisions cited notes 92, 93 *supra*. *E.g.*, MINN. STAT. ANN., § 303.09 (West 1947); N.D. REV. CODE § 10-1712 (1943).

same can be applied to foreign corporations";⁹⁵ or subjecting their directors or officers to certain liabilities similar to those that specific sections of local law impose with respect to domestic corporations.⁹⁶

Some of these provisions would, if taken literally, automatically subject all foreign-chartered corporations to local corporation law; others would similarly apply if liberally construed; nearly all would so apply if the court strained the interpretation a bit, as courts will from time to time. And yet it is inconceivable that the Mississippi courts will literally apply to a *real* foreign corporation the Mississippi statute that provides that once a foreign corporation has complied with the requirements for admission to do business in the state it "shall . . . become to all intents and purposes a corporation of this state."⁹⁷ It seems equally unlikely that the broadest interpretation, reaching all corporations, real foreign or pseudo-foreign, will be given to the Michigan provision that officers and directors of admitted foreign corporations "shall be subject to all such requirements and duties as are imposed upon officers and directors of domestic corporations organized under [the Michigan statute] . . . and shall be subject to the same penalties and liabilities for failure to perform any duties imposed by such act as are the officers and directors of domestic corporations organized thereunder."⁹⁸ Yet it is quite conceivable that under such statutes local corporation law would, on many occasions where the courts are faced with protection of local interests, be applied to pseudo-foreign corporations.

Unfortunately the statutes are not so worded as to aid the court in making the needed distinction between real and pseudo-foreign corporations. One notes, for instance, that without discussion of such a distinction, under the "no more favorable conditions" provision already mentioned,⁹⁹ a local federal court invalidated a mortgage on local property executed by the locally-operated foreign corporation without a two-thirds vote of the shareholders. The basis for the decision was that such a two-thirds requirement existed for domestic corporations and hence that this foreign-chartered—but not clearly pseudo-

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95. N.J. STAT. ANN. § 14:15-2 (1939); N.M. STAT. ANN. § 51-10-1 (1953).

96. MASS. ANN. LAWS c. 181, § 14 (1955) (liability arising out of illegal dividends, excessive indebtedness, etc.); *id.* § 17 (liability for false statements and reports); N.Y. STOCK CORP. LAW § 114, quoted *supra* note 78.

97. MISS. CODE ANN. § 5341 (1942). In *Hamilton v. United Laundries Corp.*, 111 N.J. Eq. 78, 161 Atl. 347 (Ch. 1932), the court refused to apply the local dividend statute in a suit to enjoin a dividend by a foreign corporation notwithstanding the literal language of the New Jersey statute, see text at note 95 *supra*. The extent of the local character of the corporation does not appear; it does appear, however, that the plaintiff shareholder was a non-resident.

98. MICH. STAT. ANN. c. 195, § 21.94 (Supp. 1953). For example, the Michigan General Corporation Act imposes a duty on directors not to pay dividends on common stock out of unearned surplus, and makes them liable for dividends so paid. *Id.* §§ 21.22, 21.48. Most states permit dividends on common stock out of any surplus. It is unlikely that the Michigan court (or, eventually, the United States Supreme Court) would subject directors of a non-Michigan corporation to liability despite compliance with the law of the state of incorporation simply because the corporation, though a *real* foreign one, has been admitted to do some business in Michigan.

99. See text at note 91 *supra*.

foreign corporation—should not be permitted more readily to make such a mortgage.¹⁰⁰ Still, as we have seen, such equal treatment provisions have provided the courts with a way of applying to foreign corporations seemingly quite local in character certain provisions of local corporation law relating to inspection of books and records,¹⁰¹ and of challenging elections in such corporations.¹⁰² And the background of the New York statute applying local law imposing liability for unlawful dividends on directors of foreign corporations¹⁰³ is said to have been the desire to remove the “incentive for foreign organization of domestic interests.”¹⁰⁴ Although on its face the statute purports to apply to foreign corporations in general, and although the decisions do not make it clear whether the courts will draw a line between real and pseudo-foreign corporations,¹⁰⁵ such a background does suggest that the line should be drawn.

“Hands-Off” Statutes

At the opposite extreme from the statutes just discussed there are statutory provisions in a few states that at a literal first glance seem to put the internal affairs of a foreign corporation beyond the reach of local law no matter how completely local in character is the corporation. Such a provision, found in several states, is to the effect that nothing in the local corporation act shall be construed to authorize the local state “to regulate the organization or the internal affairs of such [foreign] corporation.”¹⁰⁶

100. *Williams v. Gold Hill Mining Co.*, 96 Fed. 454 (N.D. Cal. 1899). It is by no means clear that the West Virginia corporation in question, which was operating a California gold mine, was predominantly local. Its executive headquarters appeared to be in New York, and the mortgage bonds were payable there. It is interesting, and perhaps significant, to discover that New York law at the time *also* required stockholders' two-thirds vote. 1 GEN. LAWS & OTHER GEN. STATUTES OF NEW YORK 850 (Cumming & Gilbert 1901).

But cf. *Southern Sierras Power Co. v. Railroad Comm'n*, 205 Cal. 479, 271 Pac. 747 (1928), where local law requiring a local permit for the issuance of stock by a corporation was held not to apply to a foreign corporation. No mention was made of the “no more favorable conditions” provisions. The court appeared to take an overly rigid “internal affairs” view.

101. *Toklan Royalty Corp. v. Tiffany*, 193 Okla. 120, 141 P.2d 571 (1943). See text at notes 73-75 *supra*.

102. *Hunter v. Merger Mines Corp.*, 67 Idaho 115, 170 P.2d 800 (1946). See note 76 *supra*.

103. See text at notes 78-81 *supra*.

104. *Report on Investigations of Trusts*, N.Y. S. Doc. No. 40, at 36 (1897), as quoted in KEHL, *CORPORATE DIVIDENDS* 308, n. 37 (1941).

105. See in general KEHL, *op. cit. supra* note 104, at 307-15. See also discussion *supra* pp. 143-55.

106. ILL. ANN. STAT. c. 32, § 157.102 (Smith-Hurd 1954); MO. ANN. STAT. § 351.570 (Vernon 1952); PA. STAT. ANN. tit. 15, § 2852-1001 (Purdon 1938). Since the Illinois law is the model for the American Law Institute's Model Act, this Illinois provision may spread to other states. See MODEL BUSINESS CORPORATION ACT § 99 (1953 Draft).

Georgia has a distinctive new provision requiring that “all rights and obligations as between the [foreign] corporation and its stockholders, or any class of them, and of the

Such statutes by no means foreclose the question of applicability of local law to foreign-chartered corporations, for the courts can and often do say, when faced with a pseudo-foreign corporation: this is not *really* a foreign corporation at all; its foreignness is a fiction, not substance. The only way legislation could so nail a court down as to leave it no room to look through form to substance would be by phraseology so unequivocal as to be unpalatable to the legislature. Courts can also reach the result by construing such statutes as merely codifying the general principle that the law of the state of incorporation governs the organization and the internal affairs of a corporation, together with the implicit *exceptions* to the principle.¹⁰⁷

The definition of the word "corporation" in local corporation statutes as "a corporation formed under the law of this state" (or similar phraseology) would seem to have little bearing on the problem. Such a definition only seeks to point out a basic distinction in the local corporation law—between domestic and foreign corporations generally. It should not be viewed as establishing an automatic imperviousness to local law for any foreign corporation, no matter how fictitious its foreignness. The pseudo-foreign corporation field is left, under such a provision, to case law development.

One may venture to suggest, then, that in the case of the pseudo-foreign corporation as distinguished from the real foreign corporation, such provisions seemingly putting foreign corporations beyond local law should really be no more the determinative factor than those numerous statutes previously discussed purporting to put foreign corporations under the local corporation law. Under either sort of statute courts can and do make distinctions between real and pseudo-foreign corporations in the application of local corporation law. What is lacking is only a workable formula for making the distinction.

A SUGGESTED FORMULA FOR APPLYING LOCAL CORPORATION LAW TO PSEUDO-FOREIGN CORPORATIONS

If the foregoing remarks are not too wide of the mark, the way seems open for courts to develop a formula for holding pseudo-foreign corporations subject to local corporation law.

A workable formula might start with the general proposition that matters of organization, structure and internal affairs are to be governed by the law of

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stockholders of any such corporation as between themselves, shall be determined by the laws of the home state. . . ." GA. CODE ANN. § 22-1601 (Supp. 1954).

107. An apt analogy is shareholder's liability in the case of the "thin" or "inequitably capitalized corporation." See BALLANTINE, CORPORATIONS 302-03 (rev. ed. 1946); LATTY, SUBSIDIARIES AND AFFILIATED CORPORATIONS 110-41 (1936); STEVENS, CORPORATIONS 95-99 (2d ed. 1949). If, as against the entity rule, courts have been able to work out a principle to the effect that the corporate entity may be disregarded "in any instance where a recognition of it would produce unjust or undesirable consequences," *id.* at 95, it is hard to believe that the shareholder organizing the inadequately capitalized corporation would find that his troubles vanish under a general statutory or constitutional provision (of which there are many) to the effect that shareholders shall not be liable for corporate debts.

the state of incorporation, even as to pseudo-foreign corporations. Then certain features of local corporation law would be applied on a *selective* basis. The features so selected would be not those that are merely of the enabling or blueprint variety, but those that seek to protect corporate creditors, parties dealing with the corporation, shareholders or classes or divisions of shareholders (including minority shareholders); and that in so doing reveal a strong legislative policy. Application of this formula would involve assaying the local policy, examining the local interests to be protected, and defining the pseudo-foreign corporation.

Ascertaining the Vigor of Particular Local Policies

One good touchstone of the strength of the legislative policy expressed in a particular protective feature is whether a domestic corporation could legally circumvent the feature—for instance, by an appropriate clause in its charter or by-laws. That is, if the same ends as this pseudo-foreign corporation is reaching could be attained by a domestic corporation with a properly drafted charter or by-laws, there is not much point in insisting on application of local law to the foreign enterprise. Similarly, if the local corporation statutes themselves offer ready methods for circumventing other protective features of local corporation law, there would seem to be little point in applying those protective features even to a pseudo-foreign corporation.

Indeed, some of the local provisions embodying protective features could well be viewed as of no great policy strength. In the author's view, for example, such would be the occasionally found provision requiring a specified amount of capital to be paid in before the corporation starts operating, and imposing liability for all debts incurred before this is done.¹⁰⁸ Although circumstances would vary, one can conceive of the required \$500 or \$1,000 initial capital, though presumably a feature for the protection of creditors, as being a mere drop in the bucket. Again, in some states preferred stock redemption must be made pro rata, rather than by lot. Arguably, pro rata redemption makes for equal treatment and prevents manipulations; but those advantages would seem to tip the scales only lightly, if at all, over redemption by lot, which has many aspects of practicality to recommend it.

Perhaps a guide to the strength of the policy behind a particular protective feature would be the seriousness or prevalence of the actual evils, and to a lesser degree the potential evils, against which it is aimed. Testing it by this standard we should say, for example, that the Nebraska fair-and-just statute for recapitalizations represents a strong policy choice.¹⁰⁹ So does the mandatory dividend provision of the new (although not yet in effect) North Carolina Business Corporation Act,¹¹⁰ which permits sizable shareholders under certain

108. See, *e.g.*, MODEL BUSINESS CORPORATION ACT §§ 48(g), 43(e) (1953 Draft) to the effect that a corporation is not to start business without at least \$1,000 paid in for its shares. Similar provisions, in varying amounts, are found in some 27 states.

109. See text at note 90 *supra*.

110. N.C. Sess. Laws 1955, c. 1371, § 50(i).

circumstances to force dividend payments of one-third of annual net profits. Even without a knowledge of the legislative history of such a provision we can see clearly that it purports to cope with a serious minority stockholder problem which arises frequently in close corporations—such corporations being the prevailing pattern in North Carolina.

Local Interests and the Definition of Pseudo-Foreign

Not necessarily all local strong-policy protective features need be applied to all pseudo-foreign corporations. Instead, they need be applied only when the interests sought to be protected thereby are predominantly local interests. This thought, in turn, helps to clarify something that hitherto has been left largely undefined in this discussion: what is meant by a pseudo-foreign corporation when it is not an out-and-out local enterprise, locally operating, locally managed and locally financed. A sharp eye for the predominantly local interests would lead to using the term "pseudo-foreign corporation" as merely a shorthand expression for summarizing the presence of those local interests pertinent to the *specific issue in question*. Or, to put it another way, the foreign corporation could be viewed as pseudo-foreign for one purpose, yet not necessarily so for another.

Of course a primary characteristic of the pseudo-foreign corporation would be that its main business activity takes place locally. If the main business is elsewhere, even though the shareholders or creditors may all be local residents they have undertaken to deal with an enterprise that is essentially an out-of-state one, and it would seem a little highhanded to hold such an enterprise to local corporation law. One might perhaps go a step further and concede that a corporation may properly be chartered in any state where it has substantial business contacts, whereupon it should be recognized in other states where it does business as a *real* foreign corporation, not a pseudo-foreign one. But even leaving aside the cosmopolites and the rootless, there would still be an open question as to many a Delaware corporation.

Given the predominantly local situs of the business, the *ad hoc* status of the corporation as pseudo-foreign should be determined by the predominance of the local interests among those to be protected. To illustrate: if most of the shareholders (or maybe even most of the *minority* shareholders outside the management group) are local residents, the local requirement for cumulative voting might be applied at the request of the local shareholders. Again, if one class of shares is held predominantly by local residents, the local requirement of voting by classes on fundamental changes in the charter might govern. All of which amounts to saying that for *this purpose*, the localized foreign corporation is pseudo-foreign. On the other hand, if local interests do not predominate, they might well be left to take their chances, along with the predominantly foreign members of their class, with the provisions of the law of the state of incorporation; and in such a case the corporation will not be considered pseudo-foreign.

There is judicial support for such *ad hoc* treatment of the pseudo-foreign

corporation. One recalls that in *Toklan Royalty Corp. v. Tiffany*,¹¹¹ the Oklahoma case applying the local book-inspection statute to a foreign corporation, the court said that the corporation "is not, strictly speaking, a foreign corporation *with respect to the question of examination and inspection of its books and records*."¹¹² In other words, it might well have been treated as a foreign corporation for some *other* issue, again depending on the local state's concern with the interest involved.

Application of the Local Law

Finally, if local law is to be applied, there remains the problem whether it should displace the provisions of the law of the state of incorporation or be superadded thereto. In most cases the local law, giving more protection than the foreign one, would be superadded. But it would not be fair to pick out a feature of each of the two laws on a specific matter—say, rights arising out of unlawful dividends—and by accumulation thus subject directors or shareholders to greater liability than is possible under the law of either state. In such a case the local statute, if it is to be applied, should displace the foreign one. And in the event that the foreign provision is more stringent than the local one, presumably no protective purpose would be served by choosing the more lenient local law.¹¹³ That is, if the local enterprise wants, by the foreign charter, to give even greater protection to creditor and shareholder interests, the local state can hardly object.

It has been seen that a distinction between real and pseudo-foreign corporations for purposes of applying local law is made in practice without clear judicial enunciation of the process by which it is made; and it has been shown that a rational, effective formula could without difficulty be developed and applied by the courts. It remains to examine the constitutional aspects of the suggested formula, and then to glance briefly at the way the problem is handled in the civil law countries.

CONSTITUTIONAL ASPECTS

Application to the pseudo-foreign corporation of the protective statutes that the local state has formulated for its own corporations would seem to run into

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111. 193 Okla. 120, 141 P.2d 571 (1943). See note 73 *supra* and accompanying text.

112. *Id.* at 122, 141 P.2d at 573. (Emphasis added.)

113. We may illustrate by taking the *Toklan Royalty* case, see text at note 73 *supra*, in hypothetical reverse. Suppose that Delaware had no "proper purpose" qualification to the shareholders' right to inspect the corporation's books and that Oklahoma did have such a requirement. Then, in a shareholder's suit in Oklahoma to inspect the books, the Oklahoma court most likely would have made the traditional choice of the law of the state of incorporation—unless, of course, the hypothesized Oklahoma policy *against* stockholders' inspection as of right were so strong that a charter clause granting the right unqualifiedly would have been invalid in a domestic corporation.

no serious constitutional obstacle. Non-discriminatory local requirements imposed on foreign and domestic corporations alike, otherwise constitutional as applied to domestic corporations, can constitutionally be applied to foreign corporations.¹¹⁴ Thus, the Supreme Court has held that California's former statute imposing liability to corporate creditors on the shareholders could validly subject shareholders in foreign corporations doing business in California to liability for corporate debts incurred in California.¹¹⁵ There seems to be no reason to believe that features of local corporation law other than superadded stockholder liability would run into any greater constitutional difficulty, particularly where a pseudo-foreign corporation is involved. The Court today would perhaps feel no need to resort to the fiction that the shareholders had consented to California law by taking shares in a corporation that they knew was to do business there.¹¹⁶ But such consent reasoning, if applicable at all, would apply with even greater force to a pseudo-foreign corporation than to a genuine foreign enterprise.

If, for instance, the corporation law of the local state were to adopt the policy that all shares are entitled to one vote, no more, no less, the application of this law and the consequent refusal to recognize the disfranchisement under the foreign charter of a class of shares held predominantly by its citizens in a corporation predominantly local in character would not amount, it is submitted, to denial of due process.¹¹⁷ Nor would it constitute failure to give full faith and credit to the public acts of the state of incorporation,¹¹⁸ or impairment of the obligation of contracts.¹¹⁹ All of these challenges would have to rest essenti-

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114. Indeed, the local state can exact, as the price for doing local business, that the foreign corporation reincorporate as a domestic corporation and thereby subject itself completely to local corporation law. *Railway Express Agency v. Virginia*, 282 U.S. 440 (1931).

115. *Thomas v. Matthiessen*, 232 U.S. 221 (1914); *Pinney v. Nelson*, 183 U.S. 144 (1901).

116. In the cases cited in the preceding footnote the charters themselves revealed that the corporations in question (one chartered in Colorado, the other in Arizona) were to do business in California. But there is no reason why the shareholder's knowledge need come from the charter. *But cf. Towle v. Beistle*, 97 Ind. App. 241, 186 N.E. 344 (1933), (complaint insufficient because no allegation that the defendant shareholders knew of the out-of-state operations).

117. For the use by the Supreme Court of the due process argument in reversing a state court's application of local law, see *Hartford Acc. & Indemnity Co. v. Delta & Pine Land Co.*, 292 U.S. 143, 149-50 (1934); *Home Ins. Co. v. Dick*, 281 U.S. 397, 408 (1930). See also Dodd, *The Power of the Supreme Court to Review State Decisions in the Field of Conflict of Laws*, 39 HARV. L. REV. 533 (1926). But it would seem doubtful that the local court's application of local corporation law, within the limits suggested in these pages, would amount to an unwarrantable extension of the law of the forum beyond its proper orbit (hence violative of due process), even under the "vested rights" theory of conflict of laws. See *Watson v. Employers Liab. Assurance Corp.*, 348 U.S. 66 (1954).

118. *Ibid.*

119. Even if the pseudo-foreign corporation had been admitted to do local business before the local enactment of the hypothesized voting requirements, the local state's interest in the matter under the assumed circumstances is so predominant as to bar a claim that the enactment amounts to impairment of the obligation of contract, just as is the case of a

ally upon the precarious claim that the local state has so little interest in the matter that application of its law would be unreasonable. One recalls how local law on matters fully as much within the "charter contract" was applied to a foreign corporation in the *Iowa Southern Utilities* case.¹²⁰

Departure from the easy application of the corporation law of the state of incorporation would, of course, eventually create some full faith and credit problems which would have to be solved by the Supreme Court. So far, it does not appear that the decisions of the Court compel the local state to apply the law of the state of incorporation regardless of the issue involved or of the fictitiousness of the foreign character of the corporation. True, one finds in the Court's opinions time and again expressions to the effect that membership in a corporation looks to and must be governed by the law of the state granting the incorporation,¹²¹ but the cases usually involve no conflict among the policies of the states having legitimate interests to protect, or else are cases where application of the law of incorporation was more essential to the public interest than was the discomfort to local citizens resulting from denial of local law.¹²² The most serious blow against the local state was the closely divided decision in *Order of United Commercial Travelers v. Wolfe*,¹²³ which, whatever be its soundness as applied to the cosmopolite there involved,¹²⁴ would be rather shocking if applied to a pseudo-foreign corporation.

None of the full faith and credit cases has involved the pseudo-foreign corporation. Faced with such a corporation, especially with an out-and-out

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domestic corporation. For the latter, the question would be set at rest by the usual "reserve power" clause in state constitutions or statutes. *Looker v. Maynard*, 179 U.S. 46 (1900).

120. *State ex rel. Weede v. Iowa So. Util. Co.*, 231 Iowa 784, 2 N.W.2d 372, *supplemental opinion*, 4 N.W.2d 869 (1942). See note 85 *supra* and accompanying text.

121. *Order of United Commercial Travelers v. Wolfe*, 331 U.S. 586, 624 (1947); *Modern Woodmen v. Mixer*, 267 U.S. 544, 551 (1925).

122. See *Broderick v. Rosner*, 294 U.S. 629 (1935) (local state must recognize shareholder's statutory liability imposed by state of incorporation); *Modern Woodmen v. Mixer*, 267 U.S. 544 (1925) (local court may not disregard by-laws of fraternal association incorporated in another state); *Royal Arcanum v. Green*, 237 U.S. 531 (1915) (local state must defer to law of state where fraternal beneficiary association incorporated, and cannot challenge an assessment valid under that law); *Converse v. Hamilton*, 224 U.S. 243 (1912) (local state must allow enforcement of additional shareholder liability imposed by law of state of incorporation). But see *Pink v. A.A.A. Highway Express*, 314 U.S. 201 (1941) (local state may determine for itself whether local policyholders in foreign mutual insurance company have undertaken liability for assessments upon their policies).

123. 331 U.S. 586 (1947). In this 5-to-4 decision the Court held ineffective the local South Dakota statute which invalidated contractual time restrictions upon enforcement of rights, as against the membership contract of a fraternal benefit society incorporated in Ohio containing such a restriction, despite the fact that the claim was based on an insurance certificate issued to a South Dakota resident pursuant to an application presented to the branch office in South Dakota.

124. The decision met with considerable criticism in legal periodicals. See Harper, *The Supreme Court and the Conflict of Laws*, 47 COLUM. L. REV. 883, 895-97 (1947); Notes, 57 YALE L.J. 139 (1947), 43 ILL. L. REV. 116 (1948), 21 SO. CALIF. L. REV. 187 (1948), 15 U. CHI. L. REV. 409 (1947), 33 VA. L. REV. 767 (1947).

pseudo-foreign corporation, the Supreme Court could not very well say that the matter in question "is peculiarly within the regulatory power" of the state of incorporation, "so much so that no other state can properly be said to have any public policy thereon";¹²⁵ nor, indeed, that the state of incorporation had the major concern in the issue presented.¹²⁶ The Supreme Court may use the full faith and credit clause as a rationale by which to enforce upon the state courts its view of the proper principle of conflict of laws, but it is difficult to conceive that any theory of conflicts—be it the "vested rights" theory or the "local law" theory or the "comity" theory¹²⁷—forces the local state court to acknowledge the superior interest of, say, Delaware as the charter state, in a fight among all local residents who are shareholders of a completely localized corporation.

Nor does one easily foresee the occasion for a Delaware court to "find" that the corporate enterprise in question is really Delawarian, so as to make a Delaware judgment entitled to full faith and credit in the state where the enterprise is actually localized, under some such "bootstrap doctrine" as has developed in migratory divorce law.¹²⁸ The situation in corporate controversies is not in this respect analogous to divorce law; a Delaware judgment or decree in a corporate controversy may rest, indeed, on the fact that the corporation is a Delaware corporation, but it is unlikely to involve an express or implied finding that the enterprise was "really domiciled" in Delaware.

Even if in the Supreme Court's review of the choice of law with respect to foreign corporations a guiding principle is that some matters within the corporate structure must be governed by a single law (where unreasonable con-

125. Van Devanter, J., in *Converse v. Hamilton*, 224 U.S. 243, 260 (1912).

126. Nothing in the full faith and credit concept (nor in the due process concept) requires blind adherence to a rigid rule of choice of law without regard to the major interests in the situation on the part of the competing states. It would seem just as true of corporate matters, internal or not, as of a workmen's compensation act that:

"[T]he conflict is to be resolved, not by giving automatic effect to the full faith and credit clause, compelling the courts of each state to subordinate its own statutes to those of the other, but by appraising the governmental interests of each jurisdiction, and turning the scale of decision according to their weight. . . .

" . . . .

"[California's] interest is sufficient to justify its legislation and is greater than that of Alaska, of which the employee was never a resident and to which he may never return."

Alaska Packers Ass'n v. Industrial Accident Comm'n, 294 U.S. 532, 547-50 (1935).

127. See STUMBERG, *CONFLICT OF LAWS* 6-17 (2d ed. 1951).

128. For a "good" evasive migratory divorce the parties must behave in proper legal fashion: the defendant spouse must co-operate at least to the extent of entering an appearance by attorney, or of letting himself be served in the divorcing state, whereupon the resulting decree will be entitled to full faith and credit in other states, even if the parties were not really domiciled in the divorcing state, since, under the bootstrap doctrine, the decree itself establishes the jurisdictional fact of domicile in the divorcing state, which fact is now *res judicata*, at least between the parties and their privies. *Cook v. Cook*, 342 U.S. 126 (1951).

sequences would follow from lack of uniformity),¹²⁹ still in the case of the completely localized foreign corporation that single law could perfectly well be that of the local state, except in the rare instance where this would not be just or practical. To put an extreme, and unlikely, case, suppose that local law by statute or by judicial decree compels the directors of a completely localized pseudo-foreign corporation to pay a dividend that the law of the state of incorporation forbids. It is submitted that any judgment against the directors for paying unlawful dividends under the law of the state of incorporation would not be enforceable, under the full faith and credit clause. The law that must yield may, in appropriate circumstances, as well be that of the state of incorporation as that of the local state. Of course, as the foreign corporations gradually shade off into cosmopolites, the constitutional right of any court to apply a law other than that of the state of incorporation may vanish as regards the area vaguely referred to as the internal affairs of a corporation.

A COMPARATIVE LAW VIEW

The problem under discussion is by no means unique to American law. Europeans, and particularly the French,¹³⁰ have faced it for a long time. Much of the French legal discussion has centered on the concept of the "nationality" of a corporation,¹³¹ and many authorities propound the notion that the corporation's nationality determines the "personal law" applicable to the corporation.¹³² Not all the authorities agree with this formula,¹³³ but regardless of

129. See *Order of United Commercial Travelers v. Wolfe*, 331 U.S. 586, 624 (1947); *Modern Woodmen v. Mixer*, 267 U.S. 544, 551 (1925); *Royal Arcanum v. Green*, 237 U.S. 531 (1915). See also Coleman, *Corporate Dividends and the Conflict of Laws*, 63 HARV. L. REV. 433, 460-65 (1950).

130. England apparently was the Delaware of the second half of the nineteenth century for French enterprises seeking to incorporate but to avoid the rigorous French law. In one litigated case, it appears that an attempt was even made so to anglicize the Moulin Rouge. Société "The Moulin-Rouge Attractions, Ltd.," Tribunal Correctionnel de la Seine, July 2, 1912, [1913] Dalloz Jurisprudence [hereinafter D.] II. 165. Promoters particularly liked the English legislation for its lack of requirement of an official appraisal of property transferred to the corporation for stock. They also liked the Anglo-Saxon idea of "authorized" capital, whereby with little outlay they could represent that their authorized capital was millions of francs—which, translated into French, apparently gave the empty shell the aura of a great enterprise.

131. It has been said that few questions have given rise to so much legal literature. LOUSSOUARN, *CONFLITS DE LOIS EN MATIÈRE DE SOCIÉTÉS* 80 (1949).

132. 1 COPPER ROYER, *SOCIÉTÉS ANONYMES* 532 (3d ed. 1925); 2 *id.* 19-31; 3 *id.* 147-49; 3 HOUPIN & BOSVIEUX, *SOCIÉTÉS* 222-29 (6th ed. 1928); 2 LYON-CAEN & RE-NAULT, *TRAITÉ DE DROIT COMMERCIAL* 1019-36 (5th ed. 1929); 2 ROUSSEAU, *SOCIÉTÉS COMMERCIALES* 421-31 (5th ed. 1921); SURVILLE, *DROIT INTERNATIONAL PRIVÉ* 718-29 (7th ed. 1925); Mazeaud, *De la Nationalité des Sociétés*, 55 JOURNAL DU DROIT INTERNATIONAL PRIVÉ [hereinafter CLUNET] 30 (France 1928). More recent discussion of the main lines of reasoning may be found in LOUSSOUARN, *op. cit. supra* note 131, at 81-89.

133. Some writers would discard the concept of nationality completely with respect to legal entities. Niboyet, *Existe-t-il Vraiment une Nationalité des Sociétés?*, 22 REVUE DE DROIT INTERNATIONAL PRIVÉ 402 (France 1927). See also 1 NIBOYET, *DROIT INTERNATIONAL PRIVÉ FRANÇAIS* 88-89 (2d ed. 1947); 2 *id.* 362-68 (2d ed. 1951). Others would draw a

whether the law governing the corporation was worked out through the concept of "nationality" or that of "domicile" or by a more direct route avoiding those overworked words, the determining factor in locating the corporation has turned out to be the "social seat"¹³⁴ (e.g., *le siège social, la sede amministrativa, el domicilio social, der Geschäftssitz*), which eventually won out over its nearest rival, the principal place of business (*le centre d'exploitation*).¹³⁵

The concept of the social seat is an attempt to get at the place where the "center"¹³⁶ of the corporate activities may be logically said to be—the brain or nerve center, if one may resort to anthropomorphic language. Perhaps a rough approximation, for our purposes, would be the "main office" or "executive headquarters," though these terms do not convey to Americans the importance that Europeans attach to the shareholders' meeting (*assemblée générale*), which they think of as the chief organ of the corporation, and to

distinction between public and private law in the case of "nationality." Others suggest still different systems. See LOUSSOUARN, *op. cit. supra* note 131, at 80, 90-98. But in the end, whether they work through "nationality," through "domicile" or through some other concept, they all reach substantial agreement in picking the jurisdiction that supplies the governing law. *Id.* at 98-102, 123-28.

134. 2 COPPER ROYER, *op. cit. supra* note 132, at 22-31; 3 *id.* 147; 3 HOUPIN & BOSVIEUX, *op. cit. supra* note 132, at 225 (collecting citations); 2 ROUSSEAU, *op. cit. supra* note 132, at 427; SURVILLE, *op. cit. supra* note 132, at 722. For a good discussion of the emergence of the social seat as the test, see LOUSSOUARN, *op. cit. supra* note 131, at 123-27. See list of countries that support this test in 2 RABEL, *CONFLICT OF LAWS* 33-35 (1947).

For an evaluation of the various tests, see Arminjon, *Nationalité des Personnes Morales*, ser. II, vol. 4 *REVUE DU DROIT INTERNATIONAL* 381-441 (Belgium 1902). 2 LYON-CAEN & RENAULT, *op. cit. supra* note 132, 1027-28 incline toward the principal place of business but concede that the founders may take their choice, in good faith, between that and the social seat.

The Italian CODICE CIVILE art. 2505 (1942) provides that: "Companies formed abroad having their administrative seat or the principal object of the enterprise in this country are subject to all the provisions of Italian law, even as to the requisites for the validity of the act of formation." (Emphasis added.)

135. World War I painfully showed that a concept of nationality determined by the social seat was completely inadequate for determining whether corporations can enjoy rights reserved for local nationals or escape restrictions applicable to foreigners or enemies. Accordingly, for the latter purpose a "control" test was developed, according to which the nationality of a corporation was determined by that of its control group. 2 NIBOYET, *DROIT INTERNATIONAL PRIVÉ FRANÇAIS* 364 (2d ed. 1951); Note, Niboyet [1929] *Sirey Recueil Général* [hereinafter S.] I. 121. As Niboyet points out, the single concept of nationality is inadequate to cope with the utterly different problems of conflict of laws and enjoyment of rights. For a good example of the latter, see *Société Remington Typewriter v. Kahn*, Cour de cassation [hereinafter Cass.] (Ch. req.), May 12, 1931, [1932] S. I. 57.

136. 2 COPPER ROYER, *op. cit. supra* note 132, at 23 (the brain of the corporation); 1 *id.* 534 (its "organs of will" and "organs of execution"); 3 HOUPIN & BOSVIEUX, *op. cit. supra* note 132, at 226 (where the "essential organs" and administrative works are found; where operations are planned; where the results of the activities converge); 2 LYON-CAEN & RENAULT, *op. cit. supra* note 132, at 1027 ("organs of direction"); 2 ROUSSEAU, *op. cit. supra* note 132, at 427 ("where direction is exercised and where corporate operations are decided"); SURVILLE, *op. cit. supra* note 132, at 722 ("the center of the business;" "where the company's organs function").

the place where that body's deliberations take place.¹³⁷ Despite the fact that some nice questions may arise when the shareholders' meetings, directors' meetings and corporate offices are spread over various jurisdictions,¹³⁸ the concept of the social seat seems not unworkable. It is the rare case indeed when one cannot say where the executive headquarters are or where the main office of an active corporation is, at least as between two states or countries.

Although there are doctrinal disagreements among continental legal authorities, there is unanimity on one point: the place of incorporation does not *ipso facto* determine the corporation's governing law.¹³⁹ Indeed, any suggestion

137. The text writers almost invariably mention the holding of shareholders' meetings as one of the earmarks of the social seat. See any of the writers cited in note 132 *supra*. To an American, accustomed to seeing many corporations hold their shareholders' meetings at some place in the state of incorporation that has no real business significance, and accustomed also to viewing shareholders' meetings as simply occasions to put a formal stamp of approval on what management wants to do, the European's concern with the "general assembly" seems somewhat unrealistic. However, these European "assemblies" of shareholders are, in theory at least, powerful organs (for example, in theory they determine the dividend policy); and while proxy voting is possible and not uncommon, the rubber stamp action of the shareholders is not so apparent as it is under the American system of management-prepared proxies mailed to the shareholders of record, which in effect makes management the agent of the shareholders to vote the latter's shares. This feature of voting by proxy is little used in Europe, according to my observation at a number of shareholders' meetings.

138. See LOUSSOUARN, *op. cit. supra* note 131, at 131. In *Chandora v. Fondateurs et Administrateurs de la Banque Européenne*, Tribunal Correctionnel de la Seine, Feb. 10, 1881, 8 CLUNET 158 (France 1881), the bank was incorporated in Belgium, the majority of the shares were held by French nationals, and its administrative seat (*siège administratif*) was in France. Shareholders' meetings and directors' meetings were always held in Belgium, where it also had a "considerable number" of employees, and it employed a substantial part of its capital in Belgian industries. Its securities were "issued" in both Belgium and France. *Held*, the corporation is governed by Belgian law, for that is the place of its social seat (*siège social*).

139. To show the unequivocal emphasis with which the point is made in the treatises, a few excerpts (translation ours), will suffice:

"[I]t would permit the most notorious frauds, since a quick trip to London or Guernsey would suffice to fix the company's nationality. . . . Nationality would thus depend on the founder's arbitrary will, and this is the very danger that case law . . . has sought to avoid." 2 COPPER ROYER, *op. cit. supra* note 132, at 21.

"Nationality cannot depend on the will of the founders. . . . Otherwise, it would be too easy for the founders to evade the laws that they deem too severe. . . . For the same reason the nationality of a company cannot depend, *jure soli*, on the country where . . . the formalities or organization were accomplished." 3 HOUFIN & BOSVIEUX, *op. cit. supra* note 132, at 223-24.

"French case-law has never viewed the place of formation of the corporation as the determinative element serving as a base for the applicable law. . . . Since the founders would be able to form their corporation in any country they choose, the situation would be exactly as if one applied the rule of autonomy [*i.e.*, let the incorporators arbitrarily choose the law for the corporation]." LOUSSOUARN, *op. cit. supra* note 131, at 54, 51.

"One cannot permit the founders . . . to decide at their pleasure whether the company they are forming shall be French or foreign. Otherwise, the founders could take the company out from under the provisions of the [French corporation] laws. These laws

that it should is generally dismissed quite summarily.¹⁴⁰ Of course, the place of incorporation may well, and usually does, coincide with either the social seat or some other acceptable business connection, and accordingly the law of the chartering state may be the applicable law by coincidence. But to permit the place of incorporation, per se, to furnish the law which is to govern a corporation that is by the local test an essentially local enterprise, would be simply to allow the founders to determine whether they wish to abide by local law or not.¹⁴¹ What then would be the use of embodying policy choices in the state's corporation law if that law can be so easily evaded?¹⁴² The attempt to bring the corporation's affairs, internal or other, under the law of the wrong state is viewed as a "fraud upon the law" or just plain "fraud," even though no subjective intent to evade anything or to defraud anybody is proved.¹⁴³ So if the social seat (or whatever the pertinent concept) is local, foreign incorporation does not make a corporation foreign for conflict of law purposes.

Naturally, to carry through, this system cannot permit the place stated in the charter as being the social seat¹⁴⁴ to be conclusive,¹⁴⁵ since such a place may be either completely false or else merely a paper office amounting to no more than a mailing address.¹⁴⁶ Accordingly, the designated social seat must be the real one. Furthermore, there seems to be a serious question under the Continental system whether even a *real* social seat, established in the foreign state of incorporation, when in all logic it *ought* to have been established locally,

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would thereby become a dead letter, to be evaded whenever they seem inconvenient." 2 LYON-CAEN & RENAULT, *op. cit. supra* note 132, at 1023-24.

"Nationality cannot be fixed by the laws of the place where the act of incorporation took place since thereby the founders could . . . elude the protective rules of the law. . . ." SURVILLE, *op. cit. supra* note 132, at 720.

140. See, for example, 3 PIC, *DES SOCIÉTÉS COMMERCIALES* 660 (2d ed. 1926). LOUSSOUARN points out that, unlike corporations, simple contract associations, like *associations en participation*, might well be governed by the principle of autonomy (free choice), and he cites supporting case law. LOUSSOUARN, *op. cit. supra* note 131, at 47, 50.

141. See note 139 *supra*.

142. See LOUSSOUARN, *op. cit. supra* note 131, at 41.

143. 2 COPPER ROYER, *op. cit. supra* note 132, at 24; 2 ROUSSEAU, *op. cit. supra* note 132, at 425; SURVILLE, *op. cit. supra* note 132, at 722-23. Such a case of "fraud" without subjective intent might arise with a *fictitious* social seat. 5 NIBOYET, *op. cit. supra* note 133, at 589 (1st ed. 1948).

144. European law requires designation of the social seat somewhere in the documents relating to the corporate organization or statutory publication. France, Law of July 24, 1867, art. 56 (under CODE DE COMMERCE, art. 64); Italy, CODICE CIVILE art. 2328 (1942); Spain, Law of July 17, 1951 (*Ley de Regimen Juridico de las Sociedades Anonimas*) art. 11 (*domicilio social*) BOLETIN OFICIAL, Aug. 6, 1951. Compare our frequently fictitious charter statements locating the "principal office" or "principal place of business" or "registered office."

145. 2 LYON-CAEN & RENAULT, *op. cit. supra* note 132, at 1029; 3 PIC, *op. cit. supra* note 140, at 665; 2 ROUSSEAU, *op. cit. supra* note 132, at 430.

146. The example almost invariably given by these authors (and found in the French cases) is the fictitious English office of a corporation formed under English law. The office in London of the house of Acton Dodds was, apparently, a domiciliary haven for many outside corporations. See [1924] JOURNAL DES SOCIÉTÉS 132, 134.

will succeed in making the corporation a foreign one.¹⁴⁷ Thus, suppose an enterprise otherwise thoroughly Continental were to incorporate in England, adopting articles requiring all shareholders' and directors' meetings to be held in England, and were scrupulously to adhere to those requirements. Would the Continental court, notwithstanding the Continental tradition of attaching importance to the place of those meetings as establishing the social seat, consider this an English corporation, to be governed by English law? Perhaps the case put would still give the local court a chance to wriggle out by finding the real social seat to be at the *business* offices;¹⁴⁸ so let us suppose that the promoters even go to the trouble of having the main office in England, which might not be too awkward in some businesses. Would that clinch the English nationality of the corporation even though England or Englishmen have no other substantial business contact with the enterprise? Despite an occasional voice in the affirmative,¹⁴⁹ most writers express the contrary opinion, affirming that the social seat must be not only real but also *serious*—meaning, apparently, that its fixation must respond to a serious *business* reason, not merely the desire to escape local law.¹⁵⁰ Case law seems to be in accord with this preponderant view.¹⁵¹ In one respect, however, case law appears to be more liberal than

147. 2 COPPER ROYER, *op. cit. supra* note 132, at 25; SURVILLE, *op. cit. supra* note 132, at 722-23. See also 2 ROUSSEAU, *op. cit. supra* note 132, at 425.

148. See Benoist, *Syn. de la Société Joltaia-Rieka v. Schwob*, Cour de Paris, March 23, 1909, [1909] S. II. 183, [1909] JOURNAL DES SOCIÉTÉS 268 (the "true center of initiative" of corporation organized under Belgian law to operate mines in Russia held to be in France). See also Syndicat de The Huelva Central Copper Mining Co. v. Delzens, Tribunal de Commerce de la Seine, June 29, 1910, [1911] JOURNAL DES SOCIÉTÉS 371, where the court played up the place of "administration" where books and accounts were kept and "action" took place.

149. 2 RABEL, *op. cit. supra* note 134, at 44-45; Arminjon, *supra* note 134, at 381, 408-16; Travers, *La Nationalité des Sociétés Commerciales*, 33 RECUEIL DES COURS pt. III, 70-73 (1930). Their view is that such a social seat is the real one, regardless of the motives for establishing it at that place; no fraud is involved, for it is not a case of making something look like what it is not. But, while denying any "fraud on the law," Arminjon distinguishes "fraud on the rights of third parties," which rights he would protect against evasive choice of law. See 1 ARMINJON, DROIT INTERNATIONAL 270-73 (3d ed. 1947).

150. 1 COPPER ROYER, *op. cit. supra* note 132, at 534; 2 *id.* at 25-31; 3 HOUTIN & BOUVIEUX, *op. cit. supra* note 132, at 226-27; 2 LYON-CAEN & RENAULT, *op. cit. supra* note 132, at 1029; 3 PIC, *op. cit. supra* note 140, at 665-66; 2 ROUSSEAU, *op. cit. supra* note 132, at 435; SURVILLE, *op. cit. supra* note 132, at 722-24.

Even Demogue, who favors a wide freedom of choice, is in accord. See his note in [1908] S. II. 177, 179. See LOUSSOUARN, *op. cit. supra* note 131, at 133-35, who points out, agreeing with Niboyet, that the situation under discussion presents the true case of "fraud on the law."

151. Cases squarely on the point are rare. See, however, Benoist, *Syn. de la Société Joltaia-Rieka v. Schwob*, Cour de Paris, March 23, 1909, [1909] S. II. 183, [1909] JOURNAL DES SOCIÉTÉS 268; *Mythou v. Société des Accumulateurs*, Tribunal de Commerce Seine, May 26, 1909, [1910] JOURNAL DES SOCIÉTÉS 239; *Comptoir des Caoutchoucs de Padong v. Enregistr.*, Cass., July 17, 1935, [1935] S. I. 41 (in part, the court found that the transfer of the social seat from Paris to Saigon was fictitious; but the court also mentioned the lack of any serious business tie of the company with Indo-China, since its physical operations were in Sumatra).

some of the writers, for it apparently permits the social seat to be established in any place with which there are business or personal ties, thereby allowing in many cases a considerable freedom of choice.¹⁵² Logically this view could lead to the reasonable position that once a substantial business reason exists for incorporating in a particular jurisdiction, the corporation should be governed by the law of the place of incorporation, wherever the social seat may be.¹⁵³

Once the local Continental court considers the corporation to be *really* local, though incorporated abroad, it will apply local law even to determine the validity of the enterprise's incorporation and activities. Not only are directors and officers subjected to the civil and criminal penalties of the local corporation law, but a pronouncement of "nullity" may be made by the local court¹⁵⁴ for non-compliance with local law, whatever would be the attitude of the courts of the state of incorporation.¹⁵⁵ Or if to treat the corporation as a nullity is viewed as too strong a sanction (as in some countries), the corporation may be treated as a defectively formed corporation,¹⁵⁶ which may result in unlimited liability at least for those who act for the corporation.¹⁵⁷

Perhaps Continental law goes a good deal farther than would be practicable for the United States with its numerous competing jurisdictions; and it would be no help to import the doctrinal disputes in which the European authorities have become embroiled. Still, in at least one important respect Continental

152. See *Enregistrement v. Société du Débarcadère de Cadix*, Cass., (Ch. civ.), June 20, 1870, [1870] D. I. 416 (organized in France, owned and managed by French nationals, operating docks in Spain; *held*, French, and so subject to certain French taxes); *Société West Canadian Collieries v. Vanverts*, Tribunal Civil de Lille, May 21, 1908, [1910] D. II. 41, [1908] S. II. 177, noted by Demogue.

See also *Syndicat de Société Huelva Copper Mining Co. v. Ladouce*, Cass. (Ch. req.), July 6, 1914, [1917] JOURNAL DES SOCIÉTÉS 78, where the corporation was formed in England with "social seat" in England (not explained), by Englishmen (whether mere dummy subscriber-incorporators or not does not appear) with the greater part of the shares going to Portuguese interests, to operate mines in Spain. Most of the shares were traded in the French market; eventually French directors were elected, directors' meetings were held thereafter mostly in France, and business offices were transferred to France. *Held*, corporation remains English. No real discussion of degree of original or later English interests.

153. See Note, Demogue, [1908] S. II. 177.

154. Of the many cases cited by the writers above mentioned, the following may be viewed as typical: *Société Dite Const. Ltd. v. Brown*, Cass. (Ch. civ.), Dec. 22, 1896, 24 CLUNET 364 (France 1897) (nullity); *Weber v. Société Générale Anglaise et Française*, Tribunal Commercial de Nancy, Feb. 18, 1907, 24 CLUNET 765 (France 1907) (civil liability); Tribunal Correctionnel de la Seine, Oct. 25, 1943, [1944] S. [Index] p. 60 (violation of penal law; defendants therefore ineligible under French law to be directors of this corporation, which was French in reality though incorporated abroad); *Siguier v. Fondateurs de la Banque de Marseille, Ltd.*, Tribunal Correctionnel de Marseille, Dec. 31, 1909, [1911] JOURNAL DES SOCIÉTÉS 456 (criminal liability of founders and directors, with references also to civil remedies and to nullification of the corporation).

155. See *Caro & Cie v. Société Franco-Belge de Panification Intégrale*, Tribunal de Commerce de Bruxelles, March 2, 1901, 29 CLUNET 883 and note (France 1902).

156. See HEMARD, NULLITÉS DE SOCIÉTÉS 456 (1926).

157. *Id.* at 839.

doctrine is more penetrating than ours: it invariably looks beyond the mere shell of formal incorporation to the core of business reality.

SUMMARY AND CONCLUSION

In the light of the foregoing discussion, the following summarizations and conclusions are submitted:

1. The proposition that all you have to do to escape "undesirable" features of local corporation law is to incorporate in another state having no such features is of questionable validity.

2. No fundamental principle of conflict of laws requires the forum to apply only the law of the state of incorporation to a pseudo-foreign corporation, even in matters relating to internal affairs.

3. The judicial decisions purporting to look to the chartering state for the law applicable to a foreign corporation do not by their actual holdings preclude the application of local corporation law to a pseudo-foreign corporation in a proper case.

4. Such decisions do, however, often contain unnecessarily broad statements to the general effect that the law of the chartering state governs internal matters.

5. Contrariwise, there are numerous decisions that, regardless of their actual holdings, create a body of judicial language to the effect that the foreignness, by virtue merely of outside incorporation, of a basically local enterprise is a pure fiction.¹⁵⁸

6. The conflicting verbal patterns indicated above make it possible for a court to apply local law in a proper case (or, conversely, charter-state law in a proper case) and to support such application by respectable authority.

7. Local corporation law should not be applied "in bulk" to a foreign corporation, despite the fact that it is merely a pseudo-foreign corporation; rather, only special features of local corporation law are to be applied, on a selective basis.

8. A proper case for such selective application is where there are protective features in local law reflecting a strong public policy; the interests sought to be protected by such features are, in the particular case, predominantly (or, perhaps, substantially) those of local residents; and the foreign corporation is carrying on its principal business activities locally.

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158. The student of corporation law is reminded of the verbal barrage that makes it so easy for a court to disregard the corporate entity (in a "proper" case): alter ego, buffer, blind, cloak, cover, delusion, dummy, mere fiction, mere form, mere formality, illusory mirage, screen, sham, simulacrum, subterfuge, tool. Once a euphonious verbal framework is handy, one need not be surprised to see a court use it when it is convinced that here is a proper case for looking behind corporate forms. Certainly the conflicts rule that purports to look to the chartering state for the governing law of a corporation is no more sacred than the doctrine of corporate personality.

9. The application of local law should not *require* proof that the corporation in question, otherwise basically local, was chartered outside for the very purpose of evading local law. Such proof, however, could be the clinching factor.

10. No principle of constitutional law requires the forum to apply to a pseudo-foreign corporation the law of the chartering state irrespective of the "governmental interests" of each jurisdiction.

11. It is interesting to note that other legal systems have long rejected the notion that the law of the chartering state automatically governs. Instead, there must be compliance with the law of the place where the corporation has its "social seat."

Perhaps, after all, the soundest policy to follow in incorporating a "local" enterprise is: incorporate at home.