

PRIVILEGES AND POWERS OF A CORPORATION AND THE DOCTRINE OF ULTRA VIRES

ALBERT J. HARNO

Threshing over old straw is not a particularly exhilarating pastime. The writer is aware that the subject matter here proposed is old straw, which has been worn into fine chaff through constant handling. He offers his appreciation to the gentle and courteous reader who may pursue this study, and presents as an apology for its appearance that after having taught the subject of Private Corporations for several years, and having given a moderate amount of study to it, he has evolved some theories which may be helpful. To obviate the possibility of disappointment, the writer wishes to inform the reader at the outset that there is to be found in these pages no solution of the problems relating to ultra vires acts of corporations. There follow merely some suggestions which have been found useful and convenient in the class room.

It is believed that it would be helpful to our thinking in this subject if a differentiation were made between the concepts *power* and *privilege*: it is submitted, if this were done, that a great many of the incidents of corporations which we now call *powers* would be found to be *privileges*, and that this discrimination would clarify and render more intelligible many of our problems. The concepts *privilege* and *power* are used in this study as defined by Hohfeld.¹ There is no desire nor necessity, however, because of that fact, of being drawn into a Hohfeldian controversy. Hohfeld's qualified usage of the terms has simply been found useful in making discriminations, and, after all, he has merely given these words a meaning already in common use. The concept *privilege* will henceforth in these pages be used as denoting permission. When it is said that a person is privileged in a certain line of conduct, the meaning will be that he may proceed without fear of being penalized. The concept *power* will be used to denote a situation where one person has a legal control, through the volitional exercise of which he can change the legal relations existing between him and another or between that other and a third person.²

Our thinking in this field would be simplified further, if a realistic view were taken of the nature and incidents of a corporation. Under such a view this invisible, intangible creature, which is

¹ *Fundamental Legal Conceptions* (1923) 23 et seq.

² Hohfeld, *loc. cit. supra*. See also Corbin, *Legal Analysis and Terminology* (1919) 29 YALE LAW JOURNAL, 163. The writer is aware that other legal concepts must necessarily enter into the situation. In this study, however, he wishes merely to emphasize the two mentioned.

said to have its lair only in contemplation of law, would be found to be quite mild and harmless. After all, a private corporation is but a group of individuals who have found it convenient to conduct a business through certain legal means and channels which have been made possible through the permission of that organization we call the state.³

Through this association various new legal contacts are made. The legal situation has become more complicated, as new privileges and powers have been conferred on the group through the nod of assent of that potent organization, the state. But the general scheme remains the same. Strangely enough, in speaking of the *powers* of a corporation, we ascribe their origin to the state, without thinking that all the powers, privileges, etc., possessed by a natural person are secured in a like manner.⁴

What legal rights, powers, privileges, etc., does the individual have that do not have their inception in that organization we call the state? X, an individual, has the privilege of making a contract, of defending himself, of smoking a cigar, without fear of being penalized for so doing by organized society. Now, who can say how long it will be before the smoking privilege will be withdrawn from him as has been the brimming glass? So too, X has the legal power to enter into a contract with Y and thereby to create a new obligation. This is a means of contact between individuals which organized society favors. Possibly in the years to come some great reformers may change the viewpoint of the state on this feature and the order may then well be: the individual has no legal power to enter into contracts. His situation would in this particular then be like that of a married woman at common law, or that of a monk. This new radical state may even go further and completely withdraw the privilege of making a contract, imposing a penalty for disobedience. The point is, an individual *may* do what the state permits him to do; he *can* create new legal obligations only as long as the state sanctions them; he has legal privileges and powers only through the grace of organized society.

The state organization can restrict or extend his privileges and

³ "When all is said and done, a corporation is just an association of natural persons conducting business under legal forms, methods, and procedure that are *sui generis*." Hohfeld, *op. cit.* at 198. See also *United States v. Trinidad Coal Co.* (1890) 137 U. S. 160, 11 Sup. Ct. 57.

⁴ "It is true that a corporation is a creature of the law; but so, too, are all legal rights and duties creatures of the law; and when the law creates a corporation, an artificial being, why should it not, so far as its nature permits, be capable of enjoying, and being affected by, all the rights and duties which have been previously created by the law? Why assume the necessity of another special creation of rights and duties for the corporation, supplementary to the creation of the corporation, and of rights and duties in general?" G. H. W., *Ultra Vires* (1878) 6 CENT. L. JOUR. 2, 4.

powers. Also, and this has important bearing on the discussion to follow in connection with the privileges and powers of corporations, the individual may have the legal power to do an act without the privilege. Conduct is privileged when the individual may proceed free from restraint; when he may act without incurring the disapproval of the state. With this meaning of the concept *privilege* before us, certainly it would not be contended that the individual is privileged in the commission of a crime or a tort. The frown on the countenance of the state organization is apparent. If in the concept *power* there lies the answer to what the individual can do to bring himself into new legal relations, it must also be clear that the individual can commit a tort or a crime and thus cause new legal obligations. The individual, in other words, has the legal power to create crime and tort obligations, but not the legal privilege.

When a person appoints another as his agent, he does so by the permission of the state. This is a means of contact between individuals which the state sanctions, and no penalty ordinarily will be incurred for this conduct. The individual, as a member of the organized community in which he resides, has the legal privilege of having certain acts performed for him by another. By doing this, however, he has complicated his legal relations. It is said that the principal has clothed the agent with authority to act for him. But whence comes the power of the principal to extend his activities in this manner? Must he not first have the approval of the group organization? It is found convenient to members of the group nowadays to promote intercourse by means of the principal-agent relation. But be it remembered that such a legal relation is possible only through the sanction of the organization in which we live.

This organization is to-day giving its approval to partnership associations as a legitimate mode of carrying on a business. In the efforts of our people to promote economic advancement, it has been found convenient for some to combine in what we call partnerships and thereby to utilize certain powers and privileges that do not appertain to an individual acting alone or to an individual acting through an agent. The state organization has given its sanction to this method of conducting business. It will be observed that there are certain legal burdens that attach to partnerships, but there are also legal benefits. By some it has been thought that the benefits have outweighed the burdens sufficiently to warrant their association in this manner. The doing of business with the privileges that appertain to partnership association differs only in detail from that of doing business with privileges incident to corporations.

What, then, is a corporation? A creature of the law—invisible, intangible, and existing only in contemplation of law?

Hardly all that. It is a group of individuals who have associated and organized themselves in a manner approved by the state by means of which they may enjoy certain privileges appertaining to this form of organization. There is in this theory no necessity to personify an immortal spook and to whisper of it that it often acts almost humanly. Talk of the entity doing things and of possessing powers and privileges is a mere fiction.⁵ The incidents and characteristics commonly assigned to corporations are merely privileges by means of which individuals may more fully enjoy their property.⁶

This feature, although lost sight of later, was clearly perceived by Kyd writing in 1793. He said:

"That a body framed by the policy of man, a body whose parts and members are mortal, should in its own nature be immortal, or that a body composed of many bulky, visible bodies, should be invisible, in the common acceptation of the words, seems beyond the reach of common understandings. A corporation is as visible a body as an army; for though the commission or authority be not seen by every one, yet the body, united by that authority, is seen by all but the blind: When, therefore, a corporation is said to be invisible, that expression must be understood, of the right [privilege] in many persons, collectively, to act as a corporation, and then it is as visible in the eye of the law, as any other right whatever, of which natural persons are capable; . . ."⁷

We have seen in the case of the individual that he may do certain things without fear of interference by the state. These are his privileges. As to other proposed acts the order is: if you do that, you will be penalized. As to these acts, the individual is not privileged; in fact he is under a duty not to do them. In the case of a partnership a more complex situation arises, and new privileges not appertaining to individuals acting alone, are incident to it. In the case of a corporation we have again an association of individuals with an additional and a more complicated scheme of privileges. But at the base, the two associations are quite similar.⁸ In fact, the association of the

⁵ "However, it is essential to a clear understanding of many important branches of the law of corporations to bear in mind distinctly, that the existence of a corporation independently of its shareholders is a fiction; and that the rights and duties of an incorporated association are in reality the rights and duties of the persons who compose it, and not of an imaginary being." 1 Morawetz, *Private Corporations* (2d ed. 1886) 3.

⁶ "Strangely enough, it has not always been perceived with perfect clearness that transacting business under the forms, methods, and procedure pertaining to so-called corporations is simply another mode by which *individuals* or *natural persons* can enjoy their property and engage in business." Hohfeld, *op. cit. supra* note 1, at 197.

⁷ Kyd, *Corporations* (1793) 15-16.

⁸ "A corporation like a partnership is an association of natural persons who contribute a joint capital for a common purpose, and although the

shareholders in a corporation and the relation they bear to each other is a kind of modified partnership association,⁹ the only difference being that the privileges vary in detail.

By organizing as a corporation the members escape individual responsibility to answer for the obligations of the group. This privilege (which is also a legal immunity) is enjoyed by the members of the corporation group but not by the partnership associates. Another privilege of great convenience to the corporation group lies in the fact that property may be held in a common name, and suits may be brought and defended under that name. So we might proceed with all the incidents and characteristics commonly ascribed to corporations. The point is that all of these are privileges which the associates enjoy through the permission of organized society. There is nothing artificial about it. One group finds it convenient to enjoy privileges incident to a partnership, another finds its welfare and prosperity promoted through organizing in a different way and becoming what is called a corporation. Both methods are sanctioned by the state, and both groups enjoy the privileges they have through the assent and permission of the state. The method of organization is different; the privileges of the corporation group are ordinarily set out more specifically through action of the legislature, but the ambit within which the partnership associates may act is defined scarcely less definitely through other means by which organized society makes its wishes and commands known. Under this view the so-called corporate entity resolves itself into nothing more nor less than a group of privileges possessed by individuals to do business in this manner.

The state has also conferred on the members of the corporation group certain distinct powers, that is, the ability or capacity to create new legal obligations. This legal control when possessed by an individual is called a power, but from the viewpoint of the state which sanctions, it is also a privilege. When the attitude of the state is that one may pursue a certain line of conduct without interference from the organization, we have a privilege. To the corporation group the permission is: you may take a common name, you may enter into legal obligations using this name, you may hold property in this name, the property which

shares may be assigned to new individuals in perpetual succession, yet the number of shares and amount of capital cannot be increased, except in the manner, expressly authorized by the charter or articles of association." Mr. Justice Bradley in *Railway Company v. Allerton* (1873) 85 U. S. 233, 235.

⁹ "In trading corporations the relation of the members or shareholders to one another is in fact a modified contract of partnership, which in the view of courts of equity is governed by the ordinary rules of partnership law so far as they are not excluded by the constitution of the company." Pollock, *Principles of Contract* (9th ed. 1921) 131.

you thus hold is alone subject for the debts you have incurred by means of this procedure. All these are privileges.¹⁰ Whenever the privilege involves the capacity to create new legal obligations there is associated with it a power. The making of a contract involves the exercise of both a privilege and a power.

But, as we have seen, there are legal powers which are not also privileges. Torts and crimes fall within this group. By committing an assault and battery the individual has exercised a legal power and thus has brought himself into new legal relations with another. But in no sense has society said to him: you may assault and beat others and expect no penalty for such conduct. It was failure to distinguish at this point which lead early judges and writers into error as to the capacity of a corporation to commit torts or crimes.¹¹ The argument was frequently raised in the earlier cases, since a corporation was a mere creature of the law, and since it could act only as authorized by its charter, that it could not do a wrong, because its charter did not authorize wrongs. The following line of reasoning typically represents the viewpoint of these cases:

"Corporations are the creatures of the law, of a highly refined and intangible nature, whose properties and attributes, lawyers alone can understand. Deriving their existence from the law, they must be governed by the terms of the law which creates them. They must proceed and be pursued in the path prescribed by the law. If the corporators do an act, beyond their powers, they, as individuals, and not the corporation of which they are members, must answer it. * * * Now, a corporation never was and never can be authorized by law to commit a tort; they can invest no one with power for that purpose. If, therefore, an agent constituted for a legal purpose, inflict an injury, the corporation is no more answerable than it would be for an act of that agent, done without any authority whatever derived from it, because being unauthorized to commit a wrong, it is out of the scope of its corporate powers. The act of the law, like the act of God, can work a wrong to no one, and if a man sustain damage by it, it is *damnum absque injuria*."¹²

¹⁰ Organized society may go further and create legal immunities. But even a so-called immunity is not invulnerable. If the existing social organization is overthrown and a new one installed, immunities are often found to be merely revocable privileges.

¹¹ "There are also certain privileges and disabilities that attend an aggregate corporation. * * * It can neither maintain, or be made defendant to, an action of battery or such like personal injuries; for a corporation can neither beat nor be beaten, in its body politic. A corporation cannot commit treason, or felony, or other crime, in its corporate capacity. . . ." 1 Blackstone, *Commentaries*, *476.

¹² From the argument of counsel for the plaintiffs in error in *The Chestnut Hill and Spring House Turnpike Co. v. Rutter* (1818, Pa.) 4 Serg. and R. 6, 9.

The modern view on this subject is stated by Judge Learned Hand in *United States v. Nearing* (1918, S. D. N. Y.) 252 Fed. 223, 231 as follows: "Finally, the defendants urge that a corporation cannot be guilty of

Such reasoning appeared to follow logically from the special capacity theory of a corporation. But even on that theory, it lacked discrimination; and the conclusion that the corporation was not answerable for torts and crimes, though seemingly plausible, was a *non sequitur*. The associates composing a corporation do not have the privilege any more than the individual unassociated, to commit crimes and torts, but like the individual, they have the power to do so. Mr. Chief Justice Comstock probably had this distinction in mind when he gave his opinion in the case of *Bissell v. The Michigan Southern and Northern Indiana Railroad Cos.*¹³

Once the discrimination is made between privileges and powers, a logical basis is found for the modern cases which make corporations responsible for torts and crimes.

The distinction between privileges and powers also assists in explaining the doctrine prevalent in America relating to *de facto* corporations. The *de facto* corporation is a result of imperfect organization; where in the formation of a corporation there has not been a substantial compliance with the law. It is generally held that certain circumstances must concur before the courts will recognize the doctrine. Those commonly mentioned are, a

the crime of conspiracy, or of any crime involving specific intent. This question simply turns upon how far the law has gone in imputing to a corporation the acts of its agents. Specifically it turns upon how far a publishing company, authorized to publish a pamphlet, is responsible for the acts of its officers, when actuated by the requisite intent. It is a question upon which the law has always tended towards larger and larger liability. In torts the liability is now established in the kindred case of libel (*Evening Journal v. McDermott* 44 N. J. Law, 430, 43 Am. Rep. 392), as in malicious prosecution (*Cornford v. Carleton Bank* (1839) 1 Q. B. 392). Certainly corporations may be guilty of criminal frauds. *Cohen v. U. S.* 157 Fed. 651, 85 C. C. A. 113; *Kaufman v. U. S.* 212 Fed. 613, 129 C. C. A. 149, Ann. Cas. 1916C, 466. Now, there is no distinction in essence between the civil and the criminal liability of corporations, based upon the element of intent or wrongful purpose. Each is merely an imputation to the corporation of the mental condition of its agents. It was, it is true, for long supposed that the criminal liability of corporations could not extend beyond the neglect of those positive duties imposed by law; but that depended upon the theory that acts of malfeasance being illegal must be *ultra vires*. It did not survive a more generous view of the doctrine of *ultra vires*. *Joplin Mercantile Co. v. U. S.* 213 Fed. 926, 935, 131 C. C. A. 160, Ann. Cas. 1916C, 470, a case affirmed without consideration of this question in *Joplin Mercantile Co. v. U. S.* 236 U. S. 531, 35 Sup. Ct. 291, 59 L. Ed. 705. That the criminal liability of a corporation is to be determined by the kinship of the act to the powers of the officials who commit it is true enough; but neither the doctrine of *ultra vires*, nor the difficulty of imputing intent or motive, should be regarded any longer to determine the result."

¹³ (1860) 22 N. Y. 258, 266-267. This is apparent from the following quotation taken from that case.

"One of the sources of error in reasoning upon legal as well as other questions, is, inexactness in the use of language, or, perhaps in the imperfectness of language, to express the varieties of thought. It is a self-evident truth, that a natural person cannot exceed the powers which belong to his nature. In this proposition, we use words in their literal and exact sense. In the same sense, it is a truth equally evident that a corporation cannot exceed its powers; but this is only asserting that it cannot exercise attributes which it does not possess. As an impersonal

valid law under which a corporation might be incorporated, a bona fide attempt to comply with the law, and the exercise of corporate functions.¹⁴

Where a group of individuals has formed merely a *de facto* corporation the law views it as an organization which can enter into legal obligations as well as can the corporation *de jure*.¹⁵ When it becomes a party to a legal relation, its duties can be enforced against it, and it in turn can sue to enforce its rights without fear of collateral attack on its corporate existence. Legally it differs from a *de jure* corporation only in this: it is vulnerable to a direct ouster proceeding at the instance of the state, while a *de jure* one is not.¹⁶ In terms of privileges and powers, the corporation *de facto* does not have the privilege to transact business as a corporation;¹⁷ for the state has not promised it

being, it cannot experience religious emotion, or feel the moral sentiments. Corporations are said to be clothed with certain powers enumerated in their charters or incidental to those which are enumerated, and it is also said they cannot exceed those powers; therefore, it has been urged that all attempts to do so are simply nugatory. The premises are correct when properly understood; but the conclusion is false, because the premises are misinterpreted. When we speak of the powers of a corporation, the term only expresses the privileges and franchises which are bestowed in the charter; and when we say it cannot exercise other powers, the just meaning of the language is, that as the attempt to do so is without authority of law, the performance of unauthorized acts is a usurpation which may be a wrong to the State, or, perhaps, to the shareholders. But the usurpation is possible. In the same sense, natural persons are under the restraints of law, but they may transgress the law, and when they do so they are responsible for their acts. From this consequence corporations are not, in my judgment, wholly exempt. The privileges and franchises granted are not the whole of a corporation. Every trading corporation aggregate includes an association of persons having a collective will, and a board of directors or other agency in which that will is embodied, and through which it may be exerted in modes of action not expressed in the organic law. Thus, like moral sentient beings, they may and do act in opposition to the intention of their creator, and they ought to be accountable for such acts."

¹⁴ 1 Machen, *Modern Law of Corporations* (1908) 243.

¹⁵ See Warren, *Executed Ultra Vires Transactions* (1910) 23 HARV. L. REV. 495.

¹⁶ "A *de facto* corporation is a reality. It has an actual and substantial legal existence. It is, as the term implies, a corporation. * * * It is bound by all such acts as it might rightfully perform as a corporation *de jure*. Where it has attempted in good faith to assume corporate powers; where its proceedings in that behalf are colorable, and are approved by those officers of the state who are authorized to act in that regard; where it has honestly proceeded for a number of years, without interference from the state, to transact business as a corporation; has been reputed and dealt with as a duly incorporated body, and valuable rights and interests have been acquired and transferred by it, no substantial reason is suggested why its corporate existence, in a suit involving such transactions, should be subject to attack by any other party than the state, and then only when it is called upon in a direct proceeding for that purpose, to show by what authority it assumes to be a corporation. * * * That the judgment of ouster did not and could not have a retroactive effect upon the rights of the society, and of parties who had dealt with it during its *de facto* existence, is suggested by the opinion of Wright, J., in *Gaff v. Flesher*, 33 Ohio St. 115". *Society Perun v. Cleveland* (1885) 43 Ohio St. 481, 490, 491, 497, 3 N. E. 357, 360, 364.

¹⁷ The discussion here is from the viewpoint of the state. The *de facto* corporation group owes no duty to others than the state to refrain from corporate action.

would not interfere should the group undertake to conduct itself as a corporation. The state, in fact, holds the threat of an ouster proceeding over it continually, which frequently culminates in an actual suit and a judgment of ouster. The *de facto* corporation has, however, the power to enter into legal relations,¹⁸ for all legal contracts formed before the ouster proceedings are allowed to stand and they can be enforced in the courts.¹⁹ The point is that a *de facto* corporation has the legal power to conduct itself as a corporation, but not the legal privilege.

With the formation of a corporation *de jure* the organization is no longer vulnerable in the matter of having its privilege to act as a corporation questioned; but there remain for the associates the risks and pitfalls which have been ushered in in connection with the doctrine of ultra vires.²⁰ This doctrine is a recent innovation.²¹

It would seem, however, that the view still prevails in England and in her dominions that royal charter corporations are not subject to collateral attack because of ultra vires transactions.²²

"There still, however, subsists a difference of a fundamental character between a chartered company and a company formed under a special Act or registered under the Companies Acts, and it is this: at common law a corporation created by the King's charter has power, as was determined in the *Sutton's Hospital case*,²³ to deal with its property, to bind itself by contracts, and to do all such acts as an ordinary person can do, and so complete is this corporate autonomy that it is unaffected even by a direction

¹⁸ "Consciously, or unconsciously, all courts today do treat some unauthorized corporate action as corporate action. For example: Persons have sought to become incorporated, but have failed to perform a condition precedent to incorporation. They nevertheless assume to act as a corporation. All courts, under some circumstances, treat this unauthorized corporate action as corporate action, and give legal validity to it as such." Warren, *op. cit. supra* note 15, at 497.

¹⁹ See *Society Perun v. Cleveland*, *supra* note 16.

²⁰ These vicissitudes also appertain to *de facto* organizations.

²¹ "There is no such thing as ultra vires in the case of a common law corporation * * * and it is not enacted in any statute. It affords, perhaps, the most remarkable instance in the history of English jurisprudence of the making of law by the judges; and having once been created, it is now probably saddled onto the backs of the courts, like Sinbad's Old Man of the Sea, not to be shaken off." G. H. W., *op. cit. supra* note 4, at 3. See also Buckley, *Companies and Limited Partnerships Acts* (9th ed. 1909) 11; Pollock, *op. cit. supra* note 9, at 129, 130; Green's & Brice's *Ultra Vires* (1880) 28; Warren, *op. cit. supra* note 15, at 496; Thompson, *Are Joint Stock Companies Common Law Corporations?* (1922) 42 Can. L. T. 143, 150; *Ibid.* 245; Mulvey, *The Companies Act* (1919) 39 Can. L. T. 79, 94; Blackburn, J., in *Riche v. Ashbury Ry. Carriage Co.* (1874) L. R. 9 Ex. Ch. 224, 262-264; *Bath Gas Light Co. v. Claffy* (1896) 151 N. Y. 24, 45 N. E. 390.

²² *British South African Co. v. De Beers* (1910) 1 Ch. 354; *Bonanza Creek Gold Mining Co. Ltd. v. Rex* (1916) 1 A. C. 566; *Edwards v. Blackmore* (1918) 42 O. L. R. 105; Carpenter, *Should the Doctrine of Ultra Vires be Discarded?* (1923) 33 YALE LAW JOURNAL, 49. Mr. Machen in the second volume of his excellent work on *Corporations*, pp. 823-828, questions whether this view is fully sustained.

²³ (1612) 10 Co. *1.

contained in the creating charter in limitation of the corporate powers. For the common law has always held that such a direction of the Crown—though it may give the Crown a right to annul the charter if the direction is disregarded—can not derogate from that plenary capacity with which the common law endows the company, even though the limitation is an essential part of the so-called bargain between the Crown and the corporation. * * * This feature—the unrestricted corporate capacity of the chartered company—is in marked contrast to the strict delimitation by the legislature and the Courts of the statutory or registered company to its defined objects.”²⁴

In the case of the charter corporations the situation would seem to be (as it was with the common law corporation) that these organizations have the legal power to enter into *ultra vires* transactions but not the legal privilege. The charter organization does not have the crown's permission to commit *ultra vires* acts. The crown has not said to it, you may do these acts without interference or penalty, but rather it has made it clear that if conduct *ultra vires* is indulged in both interference and penalty may be expected. But since the *ultra vires* transactions of such organizations are valid until the crown acts, it follows that the charter corporation has the power to engage in *ultra vires* undertakings. Of course, when the crown does act, the penalty to the corporation may include a cancellation of these powers.²⁵

The situation with reference to the English statutory corporation is different. In the noted case of *Ashbury Railway Carriage and Iron Co. v. Riche*,²⁶ the House of Lords held that under the Companies Acts corporations were possessed of only limited capacity and that *ultra vires* contracts did not bind the corporation. The English courts carry out this theory with severe consistency, and even a judgment by consent upon an *ultra vires* contract has been held not to be binding on the corporation.²⁷ Under this view, which appears to treat *ultra vires* acts as mere nullities, it will be observed that the corporation has neither the power nor the privilege to engage in such transactions.²⁸ It does

²⁴ Palmer, *Company Law* (10th ed. 1916) 3.

²⁵ If the discrimination made in this study between powers and privileges is correct, the phrase *ultra vires* as used in connection with corporations, is inaccurate, meaning as it does, outside or beyond the powers of the corporation. Where this expression is used in defining a corporate act, we often find the situation to be that the act is beyond both the powers and privileges of the corporation; frequently it is beyond the privileges but within the powers; but never is it beyond the powers but within the privileges.

²⁶ (1875) L. R. 7 H. L. 653.

²⁷ 2 Machen, *op. cit. supra* note 14, at 829.

²⁸ It would seem under the English authorities that an *ultra vires* contract even though fully executed is nevertheless treated as void, and that there is no quasi-contractual responsibility. This would seem to strengthen the view that, under the English holdings, there is neither the privilege nor the power to enter into *ultra vires* transactions.

not have the privilege because the ultra vires acts are outside of the express or implied privileges conferred, and it has not the power because any effort to create a legal relation of this nature is futile.

As the field of American cases dealing with ultra vires transactions is approached, the investigator is dismayed by the great confusion and want of consistency among the cases. Certain general groupings of decisions may, however, be made. The authorities quite uniformly agree, when an ultra vires contract is wholly executory on both sides, that it is not enforceable.²⁹ At the further extreme, when the contract has been fully executed on both sides, the view is that it should not be opened up or upset by the courts.³⁰ In cases where the contract has been partially performed, there is a difference of opinion. What appears to be a majority of jurisdictions hold to the view that an action can be brought on the contract.³¹ In other jurisdictions the view is maintained that no action will lie on the contract, and recovery, if any, must be had on the principles of quasi-contract.³²

Although these general classifications can be made, there remains much confusion. No American cases quite approach the position of the English decisions relative to charter corporations, where we found that the power but not the privilege existed for ultra vires undertakings. Nor do any of the American cases quite go to the other extreme set by the English cases with respect to statutory corporations, where we found that neither the privilege nor the power for ultra vires conduct was recognised. There is no definite view of the American courts, but one finds a great many views and combinations of views, which appear to hover in between the two extreme positions set by the English courts. All American courts would seem to agree that the privilege for ultra vires action does not exist. In certain federal cases a view is taken which approaches the English one relating to statutory corporations, but difficult problems are encountered in attempting to analyze the cases.

The expression is frequently found in the cases that all ultra vires contracts are *illegal* and *void*. In the language of Mr. Justice Gray:³³

“The charter of a corporation, read in the light of any general

²⁹ 2 Machen, *op. cit.* at 857-859.

But see *Harris v. Independence Gas Co.* (1907) 76 Kan. 750, 92 Pac. 1123. And see an article, Pepper, *The Unauthorized or Prohibited Exercise of Corporate Power* (1895) 9 *Harv. L. Rev.* 255.

³⁰ 2 Machen, *op. cit. supra* note 14, at 833, 843.

³¹ *Ibid.* at 851-855.

³² *Ibid.* at 840-841, 855-857.

³³ *Central Transportation Co. v. Pullman Palace Car Co.* (1891) 139 U. S. 24, 48, 11 Sup. Ct. 478, 484.

laws which are applicable, is the measure of its powers, and the enumeration of those powers implies the exclusion of all others not fairly incidental. All contracts made by a corporation beyond the scope of those powers are unlawful and void, and no action can be maintained upon them in the courts. * * *

It would seem that this language would line up the federal view alongside the English one as to statutory corporations, and that consequently there would be neither the privilege nor the power to indulge in ultra vires acts. But the words *illegal* and *void* are elusive; it is feared that they are frequently used like curse words to fill in where other language fails.

It is hoped that some one may some time give these words a thorough diagnosis. To such person, with reference particularly to the problem under discussion, the suggestion is made that an act is *void* when it does not give rise to new legal relations; when the person who does it has no legal power to create a legal obligation in that manner. If the act is simply void (but not illegal), there still is a privilege to do it, since no penalty is prescribed for it, and since there is no duty not to do it.³⁴ The situation may be quite different in the case of an *illegal* act. No legal privilege exists for it. Frequently there is neither power nor privilege for it; in that case it can be said that the act is also void. But the situation may be such that an illegal act involves legal consequences and new legal relations; in such cases there is a power to do the act, but not the privilege. All crimes and torts would certainly fall within this grouping, and there are occasionally instances in contracts where the law imposes a penalty and yet gives legal consequences to the act.³⁵ It remains to be seen whether or not the federal cases consistently maintain the position that ultra vires contracts are *illegal* and *void*.

As we have seen, the view is generally accepted that a corporation does not have the privilege of entering into ultra vires acts. It is when we come to the matter of powers that we find con-

³⁴ Possibly the want of a privilege to do the act could be found in the fact that the opposite party can bring an action to have the void act set aside. This, however, would seem merely to settle the point of the want of power to do the act, unless we found the lack of a privilege (duty not to do) in the fact that a court will assess costs. Possibly in this we could find a sufficient penalty to reason that there was no privilege to do a legally void act.

³⁵ See 3 Williston, *Contracts* (1920) sec. 1630; Anson, *Contract* (Corbin's ed. 1919) 304-307.

"Let us now concede that the unauthorized contracts of a corporation are illegal in the sense contended for. It by no means follows that they are never to be enforced. An agreement declared by statute to be void cannot be enforced because such is the legislative will. But when, without any such declaration, it is simply illegal, it is capable of enforcement where justice plainly requires it." Mr. Justice Comstock, in *Bissell v. Michigan Southern and Northern Indiana Railroad Cos.*, *supra* note 13, at 273.

fusion. If also the power does not exist, it then follows that such conduct is devoid of legal consequences, i. e., it is void. In the *Pullman* case,³⁶ Mr. Justice Gray was quoted to the effect that ultra vires contracts of corporations were void and unlawful. We appeal to him once more. In the case of *St. Louis Railroad Co. v. Terre Haute Railroad Co.*,³⁷ a suit was brought by the lessor company to set aside an ultra vires lease. The Supreme Court refused this relief. The following is a quotation from the opinion of Mr. Justice Gray:

“When the parties are *in pari delicto*, and the contract has been fully executed on the part of the plaintiff, by the conveyance of property, or by the payment of money, and has not been repudiated by the defendant, it is now equally well settled that neither a court of law nor a court of equity will assist the plaintiff to recover back the property conveyed or money paid under the contract.”³⁸

Surely, this leaves Mr. Justice Gray in a dilemma. If this decision was correct, the contract was not void and the language in the *Pullman* case was inaccurate. If the language in the *Pullman* case was accurate, the *Terre Haute* decision was wrong. It is plausible but not convincing to say that in the latter case the parties were *in pari delicto* and that in such cases the courts will refuse their aid. If the contract was actually void, i. e., that there was no power to make it, then no property could have passed under it, and the court ought to have set it aside. Possibly the contract was illegal (but not void) in the sense of there being no privilege to make it, but since the Supreme Court would not set it aside, there must have been the power to make it. This reasoning would explain the *Terre Haute* case, but in the *Pullman* case the language was that ultra vires contracts were both unlawful and void. This could mean only that there was neither privilege nor power to make them.

To reconcile these two cases and others yet to be noted we must take the position that the language in the *Pullman* case was too broad. The privilege does not exist to enter into ultra vires contracts, and in that sense these transactions may be considered illegal,³⁹ but they are not void. To sustain the *Terre*

³⁶ *Supra* note 33.

³⁷ (1891) 145 U. S. 393, 12 Sup. Ct. 953.

³⁸ *Ibid.* at 407, 12 Sup. Ct. at 956.

³⁹ Much objection has been emphasized to the use and the term *illegal* in connection with ultra vires acts of corporations, based principally on the theory that such acts are not immoral or against public policy. The writer has sympathy with this view, but believes it lacks discrimination. An ultra vires act is illegal, not because it is immoral, but because there is no privilege for it. As said by Pepper, *op. cit. supra* note 29, at 256: “Now the invalidity of an unauthorized corporate contract arises, not from the subject matter, but from the incapacity of one of the contracting

Haute case, we must assume that the legal power existed to enter into the contract, but since under the holding of the *Pullman* case (and other federal cases) this contract could be defeated before being fully executed, we must find another power in the opposite party to defeat the contract up to the time it has become fully executed. Once, though, the contract is fully executed that power ceases to exist, and the contract stands indefeasible.

In certain federal cases the reasoning approaches that of the English courts in the royal charter cases; at least it submits to the same analysis. We find particularly that no collateral attack is permitted, because of the ultra vires nature of the transaction, where the passing of title to property is involved.⁴⁰ In *National Bank v. Matthews*⁴¹ the court said:

"Where a corporation is incompetent by its charter to take a title to real estate, a conveyance to it is not void, but only voidable, and the sovereign alone can object. It is valid until assailed in a direct proceeding instituted for that purpose. * * * The impending danger of a judgment of ouster and dissolution was, we think, the check and none other contemplated by Congress. That has been always the punishment prescribed for a wanton violation of a charter, and it may be made to follow wherever the proper public authority shall see fit to invoke its application. A private person cannot, directly or indirectly, usurp this function of the government."

Since the state may interfere, the situation here is that the corporation has not the privilege to engage in these ultra vires transactions, but, since legal consequence will be given them, there is a legal power for them.

parties. It is said to be illegal, but it is illegal, not because this agreement is itself immoral, but because the law denies the corporation power [privilege] to enter into the agreement".

⁴⁰ *National Bank v. Matthews* (1878) 98 U. S. 621; *Jones v. Guaranty and Indemnity Co.* (1879) 101 U. S. 622; *Jones v. Habersham* (1882) 107 U. S. 174, 2 Sup. Ct. 336; *Reynolds v. Crawfordsville Bank* (1884) 112 U. S. 405, 5 Sup. Ct. 213; *Fritts v. Palmer* (1889) 132 U. S. 282, 10 Sup. Ct. 93; *Schuyler National Bank v. Gadsden* (1903) 191 U. S. 451, 24 Sup. Ct. 129; *Kerfoot v. Farmers' Bank* (1910) 218 U. S. 281, 31 Sup. Ct. 14; *Hagerla v. Mississippi River Power Co.* (1913, S. D. Iowa) 202 Fed. 776; *Mutual Life Ins. Co. v. Stephens* (1915) 214 N. Y. 488, 108 N. E. 856; *Puget Sound Nat. Bank v. Fisher* (1909) 52 Wash. 246, 100 Pac. 724. Cf. *California Bank v. Kennedy* (1897) 167 U. S. 362, 17 Sup. Ct. 831; *Watkins v. Iowa Cent. Ry. Co.* (1904) 123 Iowa 390, 98 N. W. 910.

In *Kerfoot v. Farmers' Bank* the court, in holding that a conveyance of land is voidable only at the instance of the state, said, "This rule, while recognizing the authority of the Government to which the corporation is amenable, has the salutary effect of assuring the security of titles and of avoiding the injurious consequences which would otherwise result." *Op. cit. supra* note 40, at 287, 31 Sup. Ct. at 15.

⁴¹ *Op. cit. supra* note 40, at 628, 629. Quoted by Warren, *op. cit. supra* note 15, at 499.

The view has been adhered to in the federal courts, where one party to an ultra vires contract has received the benefit of a performance by the other, that the latter has no remedy on the contract although the former has not performed at all.⁴² Relief, however, is frequently given to the party who has parted with consideration on the principles of quasi-contract.⁴³ While it is commonly said of these cases that the contract is void, we prefer to think, as has been pointed out, that it is not void, but that there exists up to a point a power to defeat it. Assuming then that there is a power in the defendant to defeat the contract, and so to prevent a recovery on that basis, it does not follow that the plaintiff is remediless. Aside from the defeasible power to enter into the contract, there was a distinct power for a quasi-contractual relation, and, in a proper case, recovery can be had through this channel.

While recovery is denied in the federal courts and some of the state courts on partially executed ultra vires contracts, many of the state courts permit an action in such cases on the contract itself.⁴⁴ The view of these courts is, that while the contract is wholly executory, it may be defeated, but when one party has performed and the other has not, the latter, in the interests of public policy, is not allowed to set up the defense of ultra vires. The situation here is that while there is a power to make the contract, so long as it remains wholly executory there is in the opposite party a power to defeat it, but on the performance of one party this power to defeat is extinguished in the other. The point where the contract is indefeasible is merely reached sooner in these cases than in the federal ones.

“Again, it is now settled, both at law and in equity, that a contract of a corporation, apparently within the scope of its powers, though actually beyond them, is binding on it. * * * But if a corporation has only such powers as are expressly conferred on it by its charter, and is ‘non-existent’ for all other purposes, it can not increase them by seeming to have greater. Using the same kind of logic that underlies the theory itself, it might even be said that a corporation cannot seem to have greater powers than it actually possesses, since the power of so seeming is not expressly conferred upon it. The only instance in our law, outside of corporations, where we find a physical capacity, combined with an absolute legal incapacity, to contract, is in the case of a married woman; and it is undeniably the law that the contract of a woman actually covert is absolutely void and not binding on her, though she be apparently sole, and even though she assert herself to be a *feme sole*, and the contract is

⁴² 2 Machen, *op. cit. supra* note 14, at 838-840.

⁴³ *Ibid.* at 840-841; 1 Williston, *op. cit. supra* note 35, sec. 371.

⁴⁴ 2 Machen, *op. cit.* at 851-855.

made on the faith of that statement and her apparent disclosure."⁴⁵

Such ultra vires contracts of corporations are binding even while purely executory; they furnish another instance where the state recognizes the power to enter into legal relations even though no privilege to do so has been conferred.

In conclusion, while this study was not undertaken in a reformatory spirit, certain general observations may be helpful. It is believed that much of the confusion in the cases examined has been due, first, to the notion of the special creation—the special capacity theory of corporations; and, secondly, to the effort in the interests of sound policy, to get away from the evil results of that theory. The thought is ventured that if the courts had emphasized the corporate entity and the special creation theory less, and had viewed the corporation more as a group of individuals which had certain privileges, and then had made distinction between privileges and powers, less difficulty would have resulted. The writer, while not free from doubt, believes that public policy would be promoted if the view were taken in all cases that, though a corporation may not have the privilege for ultra vires conduct, it yet should have the power for it. For this there is much precedent—more than the courts ordinarily recognize. As we have seen, precedent is to be found in certain ultra vires acts which are covered by the cloak of apparently being within the privileges and powers of the organization, in cases where partially executed contracts are enforced, in the fields where the transfer of title is involved, in cases of executed contracts, in the royal charter cases and lastly in the closely related field of *de facto* corporations. This doctrine has not worked a hardship in its application to *de facto* corporations; in fact it there seems generally to be commended. It is believed that the better view is that the allowance of a collateral attack on the corporate powers and privileges is objectionable and that it would be beneficial if the position were to be taken that such questions should be determined solely in a direct proceeding by the sovereign.

⁴⁵ G. H. W., *op. cit. supra* note 4, at 5. This comment was written before the wave of married woman's acts was well under way.