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## Corporation Executive Committees

Nancy F. Halliday\*

SOON AFTER it had been determined by the courts that management functions could be delegated by corporation boards of directors,<sup>1</sup> it became a frequent practice in business and non-profit corporations to delegate these functions to a small, active group of directors, known as the *executive committee*.<sup>2</sup> Boards of directors cannot be expected to be in session continually, and certainly the affairs of a corporation require constant supervision by some directing body.<sup>3</sup> This paper is particularly concerned with consideration of the extent to which the managerial function of the board of directors can be properly delegated to an executive committee.

### Development of Delegable Functions

It was recognized very early that the delegation of at least routine ministerial functions to executive committees was necessary for smooth and efficient management of the corporation.<sup>4</sup>

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<sup>1</sup> Hoyt v. Thompson's Exr., 19 N. Y. 207 (1859); Haldeman v. Haldeman, 176 Ky. 635, 197 S. W. 376 (1917); Maryland Trust Co. v. National Mechanics' Bank, 102 Md. 608, 63 A. 70 (1906); Sheridan Electric Light Co. v. Chatham Natl. Bank, 127 N. Y. 517, 28 N. E. 467 (1891); Young v. Canada A. & P. S.S. Co., 211 Mass. 453, 97 N. E. 1098 (1912); Tempel v. Dodge, 89 Tex. 68, 32 S. W. 514 (1895); Ballantine, Corporations, 133 (rev. ed. 1946); 19 C. J. S., Corporations, Sec. 758 (1940).

<sup>2</sup> Union Pacific Ry. Co. v. Chicago, Rock Island & Pacific Ry. Co., 163 U. S. 564, 41 L. Ed. 265 (1895); Sheridan Electric Light Co. v. Chatham Nat. Bank, *supra* n. 1; Henn, Corporations, 343 (1961); Comment, 42 Mich. L. Rev. 133 (1943). This applies also to non-profit corporations as well as to business corporations: see, Oleck, Non-Profit Corporations, Organizations & Assns., Secs. 184, 187 (2d ed., 1965).

<sup>3</sup> Ballantine, *op. cit. supra* n. 1 at 132; 2 Oleck, Modern Corporation Law, 728 (1959 with 1965 suppl.); Comment, *ibid.*

<sup>4</sup> Black River Improvement Co. v. Holway, 85 Wis. 344, 55 N. W. 418 (1893) (Committee could be delegated the authority to fix the toll rates for driving of logs); Round Lake Ass'n. v. Kellogg, 141 N. Y. 348, 36 N. E. 326 (1894); John A. Roebling's Sons Co. v. Barre & Montpelier Traction & Power Co., 76 Vt. 131, 56 A. 530, 531 (1903) (The court stated that the principle that a board of directors is the depository of discretionary powers to be exercised by the board itself, and not to be delegated by it to any smaller body, even of its own members, is entirely consistent with the other principle that it may delegate authority to perform such duties as are required in the usual and ordinary course of its business); Fensterer v. Pressure Lighting Co., 85 Misc. 621, 149 N. Y. S. 49 (1914) (Authorized delegation of ministerial, current, ordinary and routine powers); Hughes v. Cleveland Trucking Co., 2 Ohio L. Abs. 614 (Ct. App. 1924); Ohio Valley Nat. Bank

(Continued on next page)

In the case of *Fensterer v. Pressure Lighting Co.*<sup>5</sup> a statute which delegated "management of the business and affairs of the company" to the executive committee was construed by the court to mean only "ministerial, current, ordinary and routine powers" and the committee was not authorized to institute any major changes in the policies originally established by the board of directors. The executive committee in *Tempel v. Dodge*<sup>6</sup> was delegated the "full powers of the board." Here an officer and one director of the Pacific Railway Improvement Company agreed with the plaintiff's attorney to sue for the recovery of certain land, of which the plaintiff was to receive half. This contract was later approved by the executive committee, but never by the board of directors. The plaintiff sued to recover the land and the defendant contended that the contract, being approved by the executive committee, gave the plaintiff no right of action. The court stated that boards undoubtedly could appoint committees to transact the ordinary business of the corporation, but they could not confer upon others the power to discharge duties which involved the exercise of judgment and discretion.

Various other cases<sup>7</sup> have held that "ministerial" functions include execution of negotiable instruments,<sup>8</sup> making ordinary purchases on behalf of the company,<sup>9</sup> assignment of notes of a bank,<sup>10</sup> and borrowing money and giving security.<sup>11</sup> The courts' reasoning in these earlier cases was that the delegation of discretionary duties would violate the directors' duty to manage.

In later years, courts tended to become much more liberal in allowing delegation of duties which involved the use of discretion, particularly in instances where management was care-

(Continued from preceding page)

v. Walton Architectural Iron Co., 11 Ohio Dec. Reprint 904, 30 Weekly L. B. 382 (Super. Ct. of Cinc. 1893); *Gale v. Canada A. & P. S.S. Co.*, 187 F. 598 (1st Cir. 1911); *Hayes v. Canada A. & P. S.S. Co.*, 181 F. 289 (1st Cir. 1910); *Ryder v. Bushwick R.R. Co.*, 134 N. Y. 83, 31 N. E. 251 (1892); *First Natl. Bank of Binghamton v. Commercial Travelers' Home Ass'n. of America*, 108 App. Div. 78, 95 N. Y. S. 454 (1905); *Boss v. Alms & Doepke Co.*, 17 Ohio App. 314 (1923).

<sup>5</sup> *Ibid.*

<sup>6</sup> *Supra* n. 1.

<sup>7</sup> *Schwer, Delegation of Duties by Corporate Directors*, 47 Va. L. Rev. 278, 279 (1961).

<sup>8</sup> *First Natl. Bank of Binghamton v. Commercial Travelers' Home Ass'n. of America*, *supra* n. 4; *Tilden v. Goldy Mach. Co.*, 9 Cal. App. 9, 98 P. 39 (1908); *Leavitt v. Oxford & Geneva Silver Mining Co.*, 3 Utah 265, 1 P. 356 (1883).

<sup>9</sup> *Conservation Co. v. Stimpson*, 136 Md. 314, 110 A. 495 (1920); *John Roebing's Sons Co. v. Barre & Montpelier Traction & Power Co.*, *supra* n. 4.

<sup>10</sup> *Stevens v. Hill*, 29 Me. 133 (1848); *Northampton Bank v. Pepon*, 11 Mass. 288 (1814); *Schwer, op. cit. supra* n. 7.

<sup>11</sup> *In re Cincinnati Iron Store Co.*, 167 F. 486 (6th Cir. 1909).

ful to retain general supervision over the corporate activities.<sup>12</sup> In the case of *Dyer Bros. Golden West Iron Works v. Central Iron Works*<sup>13</sup> an executive committee had been formed, representing a number of corporations, which committee was delegated the power exclusively to handle any labor disputes arising with employees of the various companies over a period of three years. The court held that this was not an undue delegation of discretionary executive functions of the directors as it was merely delegation of full authority to handle one branch of the corporation's affairs. In another case, *Kennerson v. Burbank Amusement Co., Inc.*,<sup>14</sup> a contract was entered into whereby the board of directors attempted to transfer their control and management of substantially all corporate powers to the plaintiff, a member of the board. The court held that merely requiring the plaintiff to report back to the board was not sufficient retention of control on their part and the contract was void.

Numerous instances of executive committees' taking over too much power, usurping those functions which should properly remain with the board of directors, have been condemned by the courts, some as being contrary to custom and others as violating statutes requiring the board of directors to maintain control. Such was the case in *Hayes v. Canada, A. & P. S. S. Co.*<sup>15</sup> Here the by-laws, which were stated in very broad terms, purported to vest the executive committee with the "full powers of the board of directors." The plaintiff contended that this expression had no limitation at all and was a delegation of the entire powers of the corporation for an indefinite period. The plaintiff here was performing discretionary acts such as the determination of annual salaries, the amendment of by-laws and the removal of officers. The court stated in its opinion: <sup>16</sup>

It is certainly intolerable to maintain that the words "full powers" in the provision for the appointment of the executive committee, practically divested the directors of all their functions, and built up a new foundation for it in lieu of that formally established. Such an assumed absorption of the powers of the creator by the created is too absurd to receive the approbation of any court of law. \* \* \* these facts \* \* \* exhibit in a concrete way \* \* \* the impossibility of giving force to the words "full powers" in the by-law referred to except with limitations restricting them to the ordinary business transactions of the corporation.

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<sup>12</sup> Schwer, *op. cit. supra* n. 7 at 280; Oleck, *op. cit. supra* n. 3 at 729.

<sup>13</sup> 182 Cal. 588, 189 P. 445 (1920).

<sup>14</sup> *Kennerson v. Burbank Amusement Co., Inc.*, 120 Cal. App. 2d, 260 P. 2d 823 (1st Dist. Ct. App. 1953).

<sup>15</sup> *Supra* n. 4.

<sup>16</sup> *Ibid* at 293.

### Current Provisions Re Delegation

Statutory provision for executive committees is common today.<sup>17</sup> Many statutes expressly authorize delegation of authority to executive and other committees.<sup>18</sup> The Model Busi-

<sup>17</sup> Oleck, *op. cit. supra* n. 3 at 670-707, summarizing:

- Ala. Code 1958, tit. 10, Sec. 21 (29).
- Alaska Stat. 10.05.192.
- Ariz.—No statutory provision.
- Ark. Stat. 1947, Sec. 64.402.
- Calif. Corp. Code of 1947, Sec. 822.
- Colo. Rev. Stat. 1953 as amended, Sec. 31-31-7.
- Conn. Gen. Stat. 1958, Sec. 33-318 (c).
- Del. Code Ann., tit. 8, Sec. 141.
- Distr. of Columbia, D. C. Code 1961, Sec. 29-916 e.
- Fla. Stat. Ann., Sec. 608.09.
- Ga. Code Ann. Sec. 22-1867.
- Hawaii—No statutory provision.
- Idaho Code 1947—Sec. 30-139.
- Ill. Rev. Stat. 1957, ch. 32, Sec. 157.38.
- Ind. Burns' Stat. Sec. 25-208.
- Iowa Code 1962, Sec. 496 A. 39.
- Kan. Gen. Stat. 1949, Sec. 17-3101.
- Ky. Rev. Stat. 1949, Sec. 271.345.
- La. Rev. Stat. 1950, Sec. 12.34.
- Me. Rev. Stat. 1954, Ch. 53, Sec. 32.
- Md. Code 1957, Art. 23, Sec. 59.
- Mass. Gen. Laws 1932, ch. 156, Sec. 26.
- Mich. Comp. Laws 1948, Sec. 450.13.
- Minn. Stat. 1953, Sec. 301.28.
- Miss. Code 1942, Sec. 5309-77.
- Mo. Stat. 1949, Sec. 351.330.
- Mont.—No statutory provision.
- Neb. Rev. Stat. 1943, Sec. 21-114.
- Nev. Rev. Stat., Sec. 78.125.
- N. H.—No statutory provision.
- N. J. Rev. Stat. Ann. Sec. 14:7-4.
- N. M. Stat. 1953, Sec. 51-2-14.
- N. Y. Bus. Corp. Law, Sec. 712.
- N. C. Gen. Stat. (1955 Act), Sec. 55-31.
- N. D. Cent. Code Sec. 10-19-42.
- Ohio Rev. Code (1955 Act), Sec. 1701.63.
- Okl. Stat., 1951, tit. 18, Sec. 1.36.
- Ore. Rev. Stat., 57.206.
- Pa. Purdon's Stat., tit. 15, Sec. 2852-402.
- Puerto Rico Laws Ann., tit. 14, Sec. 1401.
- R. I. Gen. Laws 1956, Sec. 7-4-6.
- S. C. Code 1962, Sec. 12-18.11.
- S. D. Code 1939, Sec. 11.0707.
- Tenn. Code Ann., Sec. 48-406.
- Tex. Bus. Corp. Act of 1955, Art. 2.36.
- Utah Code Ann. 1953, Sec. 16-10-39.
- Vt. Stat. Ann., tit. 11, Sec. 223.
- Va. Code 1950 (1956 act as amended), Sec. 13.1-40.
- Wash. Rev. Code, Sec. 23.01.320.
- W. Va. Code of 1931, Ch. 31, Art. 1, Sec. 16.
- Wis. Stat. 1955, Sec. 180.36.
- Wyo. Comp. Stat. 1957, Sec. 17-36.37.

<sup>18</sup> Oleck, *ibid.*; and, Henn, *op. cit. supra* n. 2 at 343.

ness Corporation Act provides for the formation of an executive committee, defining specifically the limitations of delegation.<sup>19</sup> Provision for the appointment of executive committees is sometimes contained in the articles of incorporation, but more frequently in the by-laws.<sup>20</sup> The construction of many of these statutes and by-laws is so broad that they can easily be interpreted in many instances as allowing the boards to pass on all their authority in the management of the corporation.<sup>21</sup>

The question under consideration is how far the directors' delegation of authority should extend. Should the delegation encompass only ordinary business transactions or should it include major policy decisions such as determining officers' salaries, profit-sharing, additional compensation, amending by-laws, and declaring dividends? <sup>22</sup> It is apparent that there are matters which are so vital to the corporation's existence and involve such a high degree of discretion that only the board should act on them—decisions regarding hiring and removal of officers, determining their salaries, declaring dividends, increasing and reducing capital, borrowing money, instituting and defending suits, filling vacancies on the board, and numerous others.<sup>23</sup> Decisions in these areas should not be delegated. They are top-priority problems and certainly important enough to the welfare of the corporation that they should receive the attention of the entire board.

The solution to the problem of how far duties can be properly delegated cannot be determined by any clearly defined rules. No hard and fast line of distinction can be drawn, as is evidenced by the latitude of the delegation in various cases.<sup>24</sup> However, the purpose of an executive committee is to *aid* the board of directors in its corporate managerial duties, and the committees should not usurp those regular and vital functions which ought to remain with the board.<sup>25</sup>

It is quite probable that currently many executive committees are exceeding the authority it originally was intended they should exercise, and that they are taking over more power than

<sup>19</sup> ABA-ALI Model Bus. Corp. Act, Sec. 38; Henn, *op. cit. supra* n. 2 at 344.

<sup>20</sup> *Robinson v. Benbow*, 298 F. 561 (4th Cir. 1924); 2 *Fletcher, Private Corporations*, Sec. 549 (rev. ed. 1954); 19 *C. J. S. Corporations*, Sec. 760 (1940); *Ballantine, op. cit. supra* n. 1 at 133; *Oleck, op. cit. supra* n. 3 at 728.

<sup>21</sup> *Lattin, Corporations*, 223 (1959). *Statutes—Colo., Conn., Del., D. C., Fla., Ga., Idaho, Ind., Mich., Neb., N. J., N. C.*, *op. cit. supra* n. 17.

<sup>22</sup> *Aiken v. Insull*, 122 F. 2d 746 (7th Cir. 1941), cert. den., 315 U. S. 806, 86 L. Ed. 1205; *Ballantine, op. cit. supra* n. 1 at 133.

<sup>23</sup> *Lattin, op. cit. supra* n. 21 at 223.

<sup>24</sup> Note, *op. cit. supra* n. 7 at 297.

<sup>25</sup> *Oleck, op. cit. supra* n. 3 at 725; *Ballantine, op. cit. supra* n. 1 at 135.

has or is ever likely to be upheld by the courts.<sup>26</sup> Due to either lack of time or interest or both on the part of boards of directors, this situation frequently leads to boards becoming merely ratifying bodies which place their automatic stamp of approval on any actions taken by these committees.<sup>27</sup> The prevailing practice by committees of wielding unrestricted power in current modern corporate management operations has led to the following statement: <sup>28</sup>

Board committees . . . are often more active and of more positive influence than the boards as a whole. Their power of course stems from the tendency of boards to approve the recommendations of their committees. . . . Approval is typically almost routine in nature. As a consequence a small group on a strategic committee may wield a great deal of influence, particularly in the field of its specialty. A small finance committee, for example, was considered the main power in Armour & Co. of Illinois for a decade.

Since it remains uncertain what powers are actually conferred on executive committees by delegation of "all powers of the board," the by-laws should clearly state what powers are intended to be delegated, and the exceptions to the delegation should be specified.<sup>29</sup> Further, care should be taken that executive committees report fully and often to the boards of directors. Meetings of the full board should be scheduled frequently, and detailed and thorough consideration should be given to reports of these committees, in order to assure that the board of directors fully performs its function of managing and directing the affairs of the corporation.

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<sup>26</sup> Henn, *op. cit. supra* n. 2 at 344; Lattin, *op. cit. supra* n. 21 at 223; Mylander, *Management by Executive Committee*, 33 *Harv. Bus. Rev.* 51, 53 (May-June 1955).

<sup>27</sup> Ballantine, *op. cit. supra* n. 1 at 135.

<sup>28</sup> Temporary National Economic Committee, *Monograph No. 11, "Bureaucracy and Trusteeship in Large Corporations"* at p. 25 (1940); Lattin, *op. cit. supra* n. 21 at 224.

<sup>29</sup> Lattin, *op. cit. supra* n. 21 at 225.