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Constitutional Law: Power of a State to Exclude a Foreign Corporation Seeking to Do Intrastate Business

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STUDENT NOTES AND COMMENTS

Constitutional Law · Power of a State to Exclude a Foreign Corporation Seeking to do Intrastate Business

A corporation, being created by a single parent state, is not necessarily recognized by other states. A state is under no compulsion, constitutional or otherwise, to permit a foreign corporation to carry on any intrastate business,¹ though comity does impel most states to admit foreign corporations. The general rule is that a state may arbitrarily exclude any foreign corporation if doing so does not directly affect either interstate commerce or business of a federal nature.³

Consideration of this rule necessitates a study of the Federal Constitutional sections involved. Article IV, Sec. 2, provides:

“The citizens of each state shall be entitled to all privileges and immunities of citizens in the several states.”

The Fourteenth Amendment provides:

“ No state shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty or property without due process of law nor deny to any person within its jurisdiction the equal protection of the laws.”

Until 1868, when the Fourteenth Amendment was ratified, the main argument advanced by a foreign corporation which was seeking admission into a state was that the corporation was a citizen within the meaning of Article IV and was entitled to the privileges and immunities accorded the citizens of the several states. This theory was given no weight by the early justices of our Supreme Court, who flatly declared that a corporation is not a citizen of a state within the meaning of this clause of our Constitution.⁴ And much later, in 1928, the Supreme Court said:

¹ *Railway Express Agency v Virginia*, 282 U.S. 440, 51 Sup. Ct. 201, 75 L.E. 450 (1931) *Hemphill v. Orloff*, 277 U.S. 537, 48 Sup. Ct. 577, 72 L.E. 978 (1928).

² *Horn Silver Mining Company v New York State*, 143 U.S. 305, 314, 12 Sup. Ct. 403, 36 L.E. 164, 168, (1892) *Pensacola Telegraph Company v Western Union Telegraph Company*, 96 U.S. 1, 12-13, 24 L.E. 708, 711-712 (1878).

³ *Fidelity & Deposit Company v Brown*, 92 Vt. 390, 104 Atl. 234 (1918), see *Hooper v California*, 155 U.S. 648, 652, 15 Sup. Ct. 207, 39 L.E. 297, 299-300 (1895) (recognizes rule) Cf. *Home Owners' Loan Corporation v Stookey et ux.*, 59 Idaho 267, 81 P 2d 1096 (1938) in which the court decides that H.O.L.C. is not actually a “foreign corporation” within any state in the United States.

⁴ *Paul v. Virginia*, 75 U.S. 168, 19 L.E. 357 (1869) *Bank of Augusta v. Earle*, 38 U.S. 519, 10 L.E. 274 (1839)

"It is a settled doctrine that a corporation organized under the laws of one state may not carry on local business within another without the latter's permission, either express or implied. A corporation is not a mere collection of individuals capable of claiming all benefits assured them by Article IV, Sec. 2 of the Constitution."⁵

The Fourteenth Amendment was passed primarily to assure southern Negroes all the rights that their former masters enjoyed. It did not take corporations very long to endeavor to be included under the wide guaranties of the Fourteenth Amendment. The clauses which the foreign corporations attempted to construe to this end were due process and equal protection for persons (instead of citizens).⁶

A court need not determine whether or not a foreign corporation seeking admission is a *person* under the equal protection clause, for it can easily handle the problem in the following manner. Admitting that a state cannot deny to any person *within its jurisdiction* the equal protection of the law, a foreign corporation which has not been admitted is obviously not within the jurisdiction. Therefore, denial by the state of entrance thereto does not deprive the corporation of equal protection to any greater extent than, for instance, immigration officials deny due process in arbitrarily refusing an alien entrance into this country. An interesting application of this rule in Illinois may be found in *People v. Women's Home Missionary Society of M. E. Church*, where a testator left a legacy to a foreign corporation which had offices in Chicago and orphanages and deaconess' homes throughout the state. The state imposed an inheritance tax upon the legacy though admittedly none would have been imposed had the recipient been a domestic corporation; and it was held that, as the foreign corporation had not placed itself within the jurisdiction of the state, such taxation did not deny to any person within the jurisdiction of the state the equal protection of the law.

The equal protection clause was also considered in *Lincoln National Life Insurance Company v. Read*,⁸ where more onerous conditions were imposed upon the foreign corporation than upon domestic corporations. The Court, quoting from *Philadelphia Fire Association v. New York*,⁹ said:

Hemphill v Orloff, 277 U.S. 537, 548, 48 Sup. Ct. 577, 72 L.E. 978, 983 (1928)

⁵ Privileges and immunities reiterated, but in a different form which doesn't concern the present problem. For the distinction in the two privileges and immunities clauses, see *Slaughterhouse Cases*, 83 U.S. 36, 21 L.E. 394 (1872).

303 Ill. 418, 135 N.E. 749 (1922)

⁸ 325 U.S. 673, 65 Sup. Ct. 1220, 89 L.E. 1861 (1945)

⁹ 119 U.S. 110, 119, 7 Sup. Ct. 108, 30 L.E. 342, 347 (1886)

"The state having the power to exclude entirely has the power to change the conditions of admission at any time, for the future, and to impose as a condition the payment of a new tax, or a further tax, as a license fee [and until the corporation] pays such license fee [it] is not admitted within the state or within its jurisdiction. It is outside at the threshold seeking admission, with consent not yet given."

On the other hand, no method of handling the due process clause will circumvent a decision as to whether or not a corporation is a person. The courts hold that the liberty which is guaranteed under the Fourteenth Amendment is a liberty of natural, not artificial, persons.¹⁰ The property element of due process is more difficult. In one sense property may be considered the right to earn profits from the operation of a business, but the property of which a person cannot be deprived without due process of law under the Fourteenth Amendment does not include the right of a foreign corporation to extend its business and membership into a state which otherwise may exclude it from its boundaries.¹¹ However, if a corporation has been carrying on intrastate business or has in some manner acquired property in a state, although the state may refuse to admit the corporation, it cannot deny the corporation due process as to the property already within the state.

Of the large number of corporation cases that arise under the Fourteenth Amendment, only a few are concerned with state exclusion of a foreign corporation. In many cases there appear statements that a corporation is a person within the meaning of the due process and equal protection clauses. These cases, however, are not ones concerned with foreign corporations seeking to do intrastate business, but occur either in domestic corporation cases or where a foreign corporation is attempting to have a condition of admittance declared unconstitutional or to assert a legal right. Even here the courts are not in accord in their reasoning. For instance, in *Kentucky Finance Corporation v. Paramount Auto Exchange Corporation*,¹² a Kentucky

¹⁰ *Hague, Mayor, et al. v. Committee for Industrial Organization*, et al., 307 U.S. 496, 527, 59 Sup. Ct. 954, 83 L.E. 1423, 1443 (1939); *Western Turf Association v. Greenburg*, 204 U.S. 359, 27 Sup. Ct. 384, 51 L.E. 520 (1906); *Northwestern National Life Insurance Company v. Riggs*, 203 U.S. 243, 27 Sup. Ct. 126, 51 L.E. 168 (1906). *But see: Grosjean, Supervisor of Public Accounts of Louisiana v. American Press Company Inc., et al.*, 297 U.S. 233, 56 Sup. Ct. 444, 80 L.E. 660 (1936) (holding that under the First Amendment to the Federal Constitution a domestic corporation is entitled to protection against arbitrary state taxation)

¹¹ *National Council of the Junior Order of United Mechanics of the United States v. State Council of Virginia, Junior Order of United American Mechanics of the State of Virginia*, 203 U.S. 151, 163, 27 Sup. Ct. 46, 51 L.E. 132, 137 (1906).

¹² 262 U.S. 544, 43 Sup. Ct. 636, 67 L.E. 1112 (1923)

corporation sought to replevy an automobile wrongfully taken from it and found in Wisconsin in the possession of a Wisconsin corporation. A Wisconsin statute creating a more difficult procedure for foreign corporations which bring suits in Wisconsin courts was held invalid. The Court stated that the corporation was a person within the meaning of both the due process clause and the equal protection clause of the Fourteenth Amendment and that a nonresident corporation going into a state to recover possession of property wrongfully taken from it and brought into that state is within the protection of the Fourteenth Amendment that no state shall deny any person within its jurisdiction equal protection of the laws. However, in *Railway Company v. Whitton's Administrator*¹³ a completely different approach was used by Justice Field, who said:

"Although a corporation, being an artificial body created by legislative power, is not a citizen within the several provisions of the Constitution; yet it has been held, and that must now be regarded as settled law, that, where rights of action are to be enforced, it will be considered as a citizen of the state where created, within the clause extending the judicial power of the United States to controversies between the citizens of the different states."¹⁴

It would seem that the reasoning in the latter case, which bases the foreign corporation's right on diversity of citizenship, is far better than the reasoning in the former where the right is based upon the proposition that a corporation is a person within the Fourteenth Amendment.

Most of the cases concerning foreign corporations arise under the doctrine of unconstitutional conditions,¹⁵ and concern corporations already within the state. No small part of the controversies has been started by state jealousy of the foreign corporation's right to remove cases to a federal court on the basis of diversity of citizenship. The propositions that a state cannot condition admittance of a corporation upon its surrender of the privilege of suing in a federal court and that a state cannot exclude a foreign corporation solely because it did take a case to the federal court are too well settled to require comment.¹⁶ Virginia, nevertheless, successfully evaded a long line of decisions to this effect by requiring all foreign corporations to incorporate in Virginia before carrying on intrastate business, thereby mak-

¹³ 80 U.S. 270, 20 L. Ed. 571 (1871)

¹⁴ *Railway Company v. Whitton's Administrator*, 80 U.S. 270, 283, 20 L.E. 571. 575-576 (1871).

¹⁵ For a comprehensive discussion of this doctrine, see HENDERSON, *THE POSITION OF FOREIGN CORPORATIONS IN AMERICAN CONSTITUTIONAL LAW* (1918) Also Merrill, *Unconstitutional Conditions* (1929) 77 U. PA. L. REV. 879.

¹⁶ *Supra*, note 15.

ing it impossible for the corporations to take many of their cases to the federal courts on the basis of diversity of citizenship. The test of this constitutional provision¹⁷ came in *Railway Express Agency v. Virginia*.¹⁸ The Supreme Court, after refusing to look behind the action to see its purpose and after finding that there was no burden upon interstate commerce, held that Virginia could prevent the Railway Express Agency from carrying on intrastate business unless it incorporated there. This point seems to have been so well settled that the attorney for the corporation in *Atlantic Refining Company v. Commonwealth of Virginia*¹⁹ conceded it. More recently, in *Asbury Hospital v. Cass County*,²⁰ the Supreme Court reiterated the old, time-worn principles involved. North Dakota had passed a statute giving corporations ten years to dispose of farm lands owned by them. At the end of the period North Dakota took the property belonging to the hospital, a foreign, non-profit corporation, and sold it. The Supreme Court held the statute and the action taken under it valid, saying:

"Appellant [foreign corporation] is neither a citizen of a state nor of the United States within the protection of the privileges and immunities clauses of Art. IV Sec. 2 of the Constitution and the Fourteenth Amendment.

"The Fourteenth Amendment does not deny to the state power to exclude a foreign corporation from doing [intrastate] business or acquiring or holding property within it.

"But a state's power to exclude a foreign corporation, or to limit the nature of the business it may conduct within the state, does not end as soon as the corporation has lawfully entered the state and acquired immovable property.

"The due process clause does not guarantee that a foreign corporation when lawfully excluded as such from ownership of land in the state shall recapture its costs."²¹

These recent cases seem to follow the rules laid down in *Paul v. Virginia*²² and *Bank of Augusta v. Earle*.²³ In the latter case, which was decided more than one hundred years ago, Justice Taney, with keen foresight, wrote:

"The clause of the Constitution referred to [Art. IV Sec. 2] certainly never intended to give to the citizens of each state the privileges of citizens in the several

¹⁷ Constitution of Virginia, Sec. 163 (1902).

¹⁸ 282 U.S. 440, 51 Sup. Ct. 201, 75 L.E. 450 (1931)

¹⁹ 302 U.S. 22, 58 Sup. Ct. 75, 82 L.E. 24 (1937).

²⁰ 326 U.S. 207, 66 Sup. Ct. 61, 90 L.E. 1 (1945).

²¹ 326 U.S. 207, 66 Sup. Ct. 61, 63-64, 90 L.E. 1, 3-5 (1945).

²² 75 U.S. 168, 19 L.E. 357 (1869).

²³ 38 U.S. 519, 10 L.E. 274 (1839)

states. Besides it would deprive every state of all control over the extent of corporate franchises proper to be granted in the state; and corporations would be chartered in one, to carry on their operations in another. It is impossible upon any sound principle to give such construction to the Article in question."²⁴

The dangers that Justice Taney pointed out are perhaps more real today than then. Foreign corporations now are larger and more powerful, having a natural tendency to strangle both individual enterprise and the relatively smaller domestic corporations. A state can keep the interests of big and little business balanced only if it can completely regulate its corporations. To force a state to admit all foreign corporations and to grant them all the privileges and immunities accorded domestic corporations would be to destroy this balance and to take a big bite out of "states' rights."

Today with the exception of those corporations engaged in interstate commerce and those doing business of a federal nature, a state can arbitrarily exclude all foreign corporations. This is the proper rule if one qualification is made. A state should not be able to exclude arbitrarily a certain corporation while it admits all others of a similar nature. This does not mean that a state should not set up classes of foreign corporations—such as insurance, transportation, banking, or industrial—in the same manner in which it classified its domestic corporations. Indeed, the same classification which a state makes of its domestic corporations would be the proper one for it to use. Having established such a classification, a state need not allow a single foreign corporation of that class to enter even though many domestic corporations of the same class are carrying on business there. The state should also be permitted to set a quota if it reasonably deems one necessary

In short, the one word *arbitrarily* should be stricken from the rule, and the simplest method of accomplishing this is through judicial interpretation of the Fourteen Amendment to our Constitution.

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²⁴ 38 U.S. 519, 586-587, 10 L.E. 274, 307 (1839)