

Louisiana Law Review

Volume 2 | Number 4
May 1940

The Louisiana Business Corporation Act of 1928

Dale E. Bennett

Repository Citation

Dale E. Bennett, *The Louisiana Business Corporation Act of 1928*, 2 La. L. Rev. (1940)
Available at: <https://digitalcommons.law.lsu.edu/lalrev/vol2/iss4/4>

This Article is brought to you for free and open access by the Law Reviews and Journals at LSU Law Digital Commons. It has been accepted for inclusion in Louisiana Law Review by an authorized editor of LSU Law Digital Commons. For more information, please contact kreed25@lsu.edu.

The Louisiana Business Corporation Act of 1928

DALE E. BENNETT*

"Adam Jones—General Store," operated by the Jones family and selling everything from overalls to molasses, has given way to "Nifty Foods Company," with hundreds of stores and super stores, and to "Magnus Department Store, Inc.," covering half a city block. Similar developments in other fields of commerce and industry have necessitated a pyramiding of individual funds—the corporate form of business organization has been the answer. By this device the capital of numerous investors may be accumulated, and the individual's risk of loss is limited to the amount he chooses to contribute to the venture. The transferable nature of the shareholder's interest adds to the attractiveness of the investment and the stability of the enterprise.

The corporate franchise or privilege was originally bestowed by special legislative fiat, but by the middle of the nineteenth century general enabling statutes under which a corporation might organize were quite common in the United States. The Louisiana Constitution of 1845 expressly provided that business corporations should not be created by special laws, and that the legislature should provide general laws under which they might be organized.¹ The Louisiana Corporation Act of 1914,² a vast improvement over its predecessors,³ was rendered obsolete by a steady increase in the number, size, and complexity of corporate enterprises. More detailed rules were needed. In 1928 the Louisiana legislature enacted a comprehensive business corporation statute⁴ and became the first state to adopt the Uniform Business Corporation Act, approved by the National Conference of Com-

* Assistant Professor of Law, Louisiana State University.

1. La. Const. of 1845, Art. 123. A similar provision is found in La. Const. of 1921, Art. IV, § 4.

2. La. Act 267 of 1914.

3. Previous corporation statutes were very limited and inadequate. La. Act 100 of 1848; La. Act 111 of 1882; La. Act 36 of 1888; La. Act 78 of 1904.

4. La. Act 250 of 1928 [Dart's Stats. (1939) §§ 1080-1154]. The provisions of this act are applicable, in general, to existing corporations. La. Act 250 of 1928, § 68 [Dart's Stats. (1939) § 1148].

missioners on Uniform State Laws in that year.⁵ The draftsmen of the Louisiana statute made several major changes, which will be hereinafter noted, together with numerous minor alterations in phraseology. On the whole, however, they followed the Uniform Act both as to format and substance. This statute, expressly labelled the *Business Corporation Act*,⁶ provides for the formation of corporations for any lawful businesses, except those of banking and insurance, and homestead or building and loan associations.⁷

The purpose of this discussion of the Louisiana Business Corporation Act shall be two-fold: First, to collect and critically analyze judicial decisions construing the Louisiana statute or other statutes similarly patterned after the Uniform Act; and Second, to provide a general survey and bird's-eye view of the Louisiana Act, with the hope of indicating some of its possibilities, and to offer a few suggestions as to the formation and operation of a business corporation.⁸

FORMATION OF THE CORPORATION

Section 2⁹ of the Act permits incorporation by three or more natural persons,¹⁰ who must be either of full age or relieved of

5. 9 U.L.A. 38 (Perm. ed. 1932). According to the note in 9 U.L.A. 29 (Supp. 1938), only two other states can be considered as having adopted the Uniform Act. Idaho adopted about half of the act verbatim and a large number of other sections with changes. Idaho Laws of 1929, c. 262, Idaho Code Ann. (1932) §§ 29-101 to 29-164. The other state listed is Washington. Washington Laws of 1933, c. 185, Wash. Rev. Stat. Ann. (Remington, Supp. 1933) §§ 3803-1 to 3803-68. A number of states have enacted comprehensive modern corporation laws. Cal. Civ. Code (Deering, 1931) §§ 277-413 (enacted in 1931); Ill. Rev. Stat. Ann. (Smith-Hurd, 1935) c. 32, § 157.1-157.167 (enacted in 1933); Ind. Stat. Ann. (Burns, 1933) §§ 25-101 to 25-254 (enacted in 1929); Mich. Comp. Laws (Mason, Supp. 1935) §§ 10135-1 to 10135-193 (enacted in 1931); Minn. Stat. (Mason, Supp. 1936) §§ 7492-1 to 7492-61 (enacted in 1933); Ohio Gen. Code Ann. (Page, Supp. 1935) §§ 8623-1 to 8623-167 (enacted in 1929); Pa. Stat. (Purdon, 1936) tit. 15, §§ 2852-1 to 2852-1202 (enacted in 1933 and amended in 1935); Tenn. Code Ann. (Williams, 1934) §§ 3714-3771 (enacted in 1929).

6. La. Act 250 of 1928, § 73 [Dart's Stats. (1939) § 1153].

7. Id. at § 2 [Dart's Stats. (1939) § 1081]. In *Mouton v. First Nat. Life Ins. Co.*, 177 So. 431 (La. App. 1937), the court held that since an insurance company could not be formed under the Business Corporation Act, its provisions were inapplicable to such a corporation.

8. In predicting the probable scope and meaning of those numerous sections of the act which are yet to be exposed to the fire of judicial determination, the writer has relied largely upon law review articles, treatise materials and the Commissioners' Notes to the Uniform Business Corporation Act, 9 U.L.A. (Perm. ed. 1932). Prior decisions of Louisiana and common law courts also serve as valuable guides, indicating the fundamental purpose and nature of the rules codified, altered or repealed, as the case may be, by the new statutory provisions.

9. La. Act 250 of 1928, § 2 [Dart's Stats. (1939) § 1081].

10. The term "persons" in earlier Louisiana corporation statutes was construed to mean "natural persons" and not to include a corporation. Fac-

minority disabilities by emancipation. There is no requirement of residence or citizenship,¹¹ although it is necessary that the incorporators be shareholders.¹² Such requirements have never served any practical purpose, for it is always possible for out-of-state promoters to secure local residents as dummy incorporators and to furnish them with the requisite qualifying shares. Later, after the corporation is fully organized, the nominal incorporators transfer their shares back to the true owners and drop out of the picture. Similarly, the minimum requirement of three incorporators presents no serious obstacle to the individual desiring to incorporate his business. Members of the family or the office force of the attorney handling the matter are usually drafted as nominal organizers.¹³

The Articles of Incorporation, which must be executed by authentic act signed by each of the incorporators, or his duly authorized agent, provide the framework of the corporation. They should be drawn carefully, so as to comply with all requirements of the Act and to effectuate the true purpose of the organizers.

Section 3¹⁴ enumerates those matters which must be stated in the articles. It is to be noted that a corporation is not limited to a single purpose.¹⁵ Thus, the required purpose clause may expressly include all business activities in which the corporation is likely to engage. It is preferable that such additional purposes be

tors & Traders' Ins. Co. v. New Harbor Protection Co., 37 La. Ann. 233, 238 (1885).

An exception is made in cases of consolidation. La. Act 250 of 1928, § 49 [Dart's Stats. (1939) § 1129] provides that the constituent corporations may be named as incorporators in the articles of the new consolidated corporation.

11. A limitation found in La. Act 267 of 1914, § 1, that "where there are only three incorporators husband and wife can not be two of such incorporators," is omitted from the new provision.

The Uniform Business Corporation Act, § 2, 9 U.L.A. 42 (Perm. ed. 1932), requires that the incorporators be "citizens of the United States or its territories," but contains no residence requirement.

12. Section 3, I(d) requires each incorporator to subscribe for at least one share.

13. The legal entity of a *one-man corporation* is generally recognized. *Salomon v. Salomon & Co.* [1897] A.C. 22 (the owner's wife and children were nominal associates); but the sole owner must act honestly and actually maintain the corporate business separate and distinct from his individual affairs. *Gordon v. Baton Rouge Stores Co.*, 168 La. 248, 121 So. 759 (1929).

14. La. Act 250 of 1928, § 3 [Dart's Stats. (1939) § 1082].

15. *Id.* at § 3, I(a) [Dart's Stats. (1939) § 1082, I(a)]. For an interesting discussion of the "blank check" available to the draftsman of a corporate purpose clause, and its effect upon the "fading star of ultra vires," see Smith, *Review of Cases on Corporations by Ballantine and Lattin* (1940) 6 O.S.L.J. 240, 242.

expressly stated, rather than to rely on the expectation that they will be regarded as implied from, or incidental to, some stated purpose.

The duration of the corporation must be set forth.¹⁶ The Act contains no limitation in this respect, but the corporation may not be given perpetual existence.¹⁷ Where the period of existence stated in the articles has elapsed, and there has been no amendment thereto, the corporation ceases to exist even as a *de facto* corporation.¹⁸

The articles should furnish a general outline of the financial structure of the corporation. They must set out the authorized number of shares; the classification, preferences, rights, or restrictions of the several classes of shares; and the amount of paid-up capital with which the corporation will begin business.¹⁹ It is also required that the place of the corporation's registered office, the names and addresses of its registered agents, and the name and address of each incorporator, with the number of shares subscribed for by him, shall be stated in the articles.²⁰ The states are about evenly divided between the practice of naming the first directors in the articles and having them elected after incorporation.²¹ The Louisiana Act leaves it optional with the incorporators, either to name the first directors or to provide a place where, and a date (not more than 60 days after execution of the articles) when, the shareholders shall meet and elect the first directors.²² Special provisions may be included dealing with preemptive rights, dividends of "wasting asset" corporations, et cetera.²³

Section 4, subsection I²⁴ requires that the corporate name, which must be stated in the articles,²⁵ shall indicate a corporate

16. La. Act 250 of 1928, § 3, I(b) [Dart's Stats. (1939) § 1082, I(b)]. Ninety-nine years is the duration generally provided for.

17. La. Const. of 1921, Art. 13, § 7.

18. *Screwman's Benev. Ass'n of Louisiana v. Monteleone*, 168 La. 664, 123 So. 116 (1929), holding that a corporation, which had continued business after expiration of its charter, was without corporate capacity and could not sue for specific performance of a contract. See also 8 *Fletcher, Corporations*, § 3842.

19. La. Act 250 of 1928, § 3, I(e)-(g) [Dart's Stats. (1939) § 1082, I(e)-(g)].

20. *Id.* at § 3, I(c), (d), (i) [Dart's Stats. (1939) § 1082, I(c), (d), (i)].

21. Commissioners' Notes to the Uniform Business Corporation Act, 9 U.L.A. 44 (Perm. ed. 1932). The Uniform Business Corporation Act, § 3, I(g), requires the naming of the first directors in the articles.

22. La. Act 250 of 1928, § 3, I(h) [Dart's Stats. (1939) § 1082, I(h)].

23. *Id.* at § 3, II [Dart's Stats. (1939) § 1082, II]. These provisions will be particularly discussed in connection with subsequent sections of the act.

24. *Id.* at § 4, I [Dart's Stats. (1939) § 1083, I].

25. *Id.* at § 3, I [Dart's Stats. (1939) § 1082, I].

existence by ending with the word *Corporation*, the word *Incorporated*, or the abbreviation *Inc.* Subsection II prohibits the assumption of a name "deceptively similar to the name of any other domestic corporation or of any foreign corporation authorized to do business in this state." A very liberal interpretation of the term "deceptively similar" was adopted by the Louisiana Supreme Court in the recent case of *State v. Conway*,²⁶ which involved a similar statutory limitation on the names of foreign corporations seeking to do business in the state. It was there held that a Tennessee corporation, the "Equitable Securities Corporation," by adding the term "of Nashville" to its name, had sufficiently distinguished itself from "Equitable Securities Company, Inc.," a domestic corporation.

The protection afforded by the dissimilarity-of-name requirement of the Act is considerably broader than the protection available under general common law rules, in which mere identity or similarity of names is not regarded as a sufficient basis for relief.²⁷ Subsections III and IV further enlarge upon the common law by furnishing an opportunity for a person or unincorporated association anticipating incorporation within a year, or of a foreign corporation planning to extend its operations into the state within such period, to secure advance protection of its trade name by filing a notice of intention with the Secretary of State.²⁸ This advance protection expires twelve months from the date of filing

26. 189 La. 272, 179 So. 312 (1938). See discussion of decision, *Work of Louisiana Supreme Court*, I LOUISIANA LAW REVIEW 314, 406 (1939).

27. "The object of subdivisions III and IV is to supplement other protection afforded by law in the use of trade or corporate names. In the absence of statutory provision, an individual or corporation may obtain injunctive relief against the use of his or its name both because of the injury to his or its property right in the name, and because of the possible deception of the public by the use of the name. But the mere identity or similarity of names does not furnish ground for relief; there must be either (a) probable deception of the public, or (b) an appropriation of a property right in a name." Commissioners' Notes to Section 4 of the Uniform Business Corporation Act, 9 U.L.A. 46 (Perm. ed. 1932). Section 4, III and IV, of the Louisiana act is substantially the same as Section 4, III and IV, of the Uniform Business Corporation Act.

28. Subdivisions III and IV give opportunity for advance protection to one who anticipates an expansion in business. For example, a baking company can acquire an exclusive right to a name under the common law, only in the locality in which it has operated; it may not be able to operate over the whole United States in one year, but may be able to expand gradually. In the meantime, its expansion may be balked if an outsider appropriates its name, subsequent to its original use by the baking company but prior to its use by the baking company in this new field. [See *Sweet Sixteen Co. v. Sweet '16' Shop*, 15 F. (2d) 920 (C.C.A. 8th, 1926)]. Subdivisions III and IV are intended to supplement the case law in this respect. Commissioners' Notes to the Uniform Business Corporation Act No. 3, 9 U.L.A. 47 (Perm. ed. 1932).

of the notice, and it is expressly provided that "such notice once given cannot be renewed." The above provisions supplement, but do not supersede, the general principles of law and equity relative to unfair competition in the use of trade names. Subsection V expressly declares that nothing in the section shall be construed as abrogating, limiting, or derogating from those principles.

Subsection VIII provides that the assumption of a name in violation of the section shall not affect or vitiate the corporate existence, but the state or party affected may enjoin the corporation from doing business under the improper name. In Alabama a similar result has been reached without express statutory declaration.²⁹ Inclusion of the provision, however, was a wise precautionary measure. It forestalls the possibility that assumption of an unlawful corporate name might be considered a defect in incorporation. At the same time it points the way to the proper remedy by way of injunctive relief.

After the articles are drafted, the procedure for incorporation is relatively simple. Section 5³⁰ provides that the articles "shall be recorded with the Recorder of Mortgages of the parish in which the registered office is situated;" and such recording is designated as the exact point in the procedure of organization where "the corporate existence shall begin."³¹ Next, a certified copy of the articles, bearing proper evidence of recording should be delivered to the Secretary of State. It then becomes the ministerial duty of that officer to issue a certificate of incorporation setting out the date and hour when the articles were recorded and at which corporate existence began.

PRE-INCORPORATION SUBSCRIPTIONS AND SHAREHOLDER LIABILITY

Pre-incorporation subscriptions were treated by a majority of the early cases as mere continuing offers by the subscribers to the

29. *State v. Citizens' Light & Power Co.*, 172 Ala. 232, 238-239, 55 So. 193, 195 (1911). Anderson, J., declared: "After he [the probate judge charged with recording the certificates] accepts the name and records the certificate, we do not think that the similarity of the name would of itself forfeit or authorize the vacation of the charter.

The provision was evidently intended to protect existing corporations from an interference with their name or business, and an injured one would no doubt have the right to enjoin the use of the name by the new corporation."

30. La. Act. 250 of 1928, § 5 [Dart's Stats. (1939) § 1084].

31. Under the Uniform Act, the corporate existence does not begin until the certificate of incorporation is issued by the Secretary of State. Uniform Business Corporation Act, § 5, II, 9 U.L.A. 48 (Perm. ed. 1932).

proposed corporation, which might be withdrawn at will and did not become binding until acceptance by the corporation after its formation.³² On the other hand, a substantial number of courts took the view that such subscriptions were of a two-fold nature and constituted: (1) binding and irrevocable contracts between the several subscribers to take shares in the proposed corporation, and (2) continuing offers which the corporation, upon coming into existence, might accept and make the subscribers shareholders.³³ The result achieved by the second line of decisions was socially desirable, for it is to the interest of each subscriber that all others be bound, and it is to the interest of the public that new corporations should have enforceable subscriptions as resources. The Louisiana Business Corporation Act carries forward the idea that pre-incorporation subscriptions should be irrevocable. Section 6, subsection I,³⁴ declares that, unless otherwise provided in the writing,³⁵ such subscriptions shall be irrevocable for a period of one year from the date of signing. After that period subscriptions may be revoked unless corporate existence has begun. With the beginning of corporate existence, those who have subscribed for shares automatically become shareholders, pursuant to an express provision in Section 5, subsection I. No further act or acceptance by the newly formed corporation is required. The general right to avoid the subscription on grounds which would be sufficient for the rescission of a contract is expressly reserved.³⁶ A subscription procured by fraud, duress, or undue influence may be rescinded, provided that the subscriber has not been guilty of laches in discovering the fraud or in repudiating the subscription after the discovery; and provided further that the rights of subsequent corporate creditors will not be affected.³⁷

32. The leading case of *Bryant's Pond Steam-Mill Co. v. Felt*, 87 Me. 234, 32 Atl. 888 (1895) was followed in *Vermilion Sugar Co. v. Vallee*, 134 La. 661, 64 So. 670 (1914). For a full collection of cases see 13 Am. Jur. 333, n. 14, § 227; 4 Fletcher, Corporations, 91, § 1425.

33. *Shelby County Ry. v. Crow*, 137 Mo. App. 461, 119 S.W. 435 (1909); *Nebraska Chicory Co. v. Lednicky*, 79 Neb. 537, 113 N.W. 245 (1907).

34. La. Act 250 of 1928, § 6, I [Dart's Stats. (1939) § 1086, I].

35. *Ibid.* It is expressly required that the subscription "shall be in writing." However, in *Jackson Fire & Marine Ins. Co. v. Walle*, 105 La. 89, 29 So. 503 (1900), a director who had his name put on the corporate books as a subscriber for a number of shares was *estopped* to assert that he never intended to purchase the shares and that no written subscription was executed; and was held liable to an extent necessary to pay corporate debts.

36. La. Act 250 of 1928, § 6, II [Dart's Stats. (1939) § 1086, II].

37. In *Hunsicker v. Gilham*, 163 La. 651, 112 So. 518 (1927), the shareholder had not been guilty of laches and there were no subsequent creditors. Rescission was allowed. Accord: *Gress v. Knight*, 135 Ga. 60, 68 S.E. 834

After the subscriber's status as a shareholder becomes established by the formation of the corporation, the latter may enforce the subscription according to its terms; and where no time of payment is stated, the shares are to be paid for on the call of the board of directors.³⁸ In case of default in payment, subsection IV of Section 6, states that, in addition to the usual remedies available, the corporation may sell the shares at public auction, provided that it can get a bid of a sum sufficient to cover the unpaid balance. Where no such bid is secured, the corporation may forfeit any payments made by the delinquent shareholder to itself as liquidated damages, and the shares shall be considered as unissued and unsubscribed.³⁹ As a further means of enforcing the delinquent shareholder's obligation, Section 22⁴⁰ gives the corporation a lien upon shares for any unpaid balance of the purchase price. Under Section 15 of the Uniform Stock Transfer Act, adopted in Louisiana,⁴¹ the validity of such a lien is dependent upon the corporation's keeping possession of the share certificates. Also, Section 16⁴² of the Business Corporation Act prohibits the issuance of a share certificate until the shares represented are fully paid for. However, in *Minden Syrup Company v. Applegate*,⁴³ a corporation, suing an original shareholder to recover the balance due on stock issued for property at an excessive valuation, was held to have a lien upon such stock and to be entitled to a writ of sequestration to prevent the shareholder from disposing of the stock pending suit.⁴⁴

CONDITIONS PRECEDENT TO BEGINNING BUSINESS

It is highly desirable, for the protection of those dealing with the corporation, that a definite fund should be established in the corporate treasury before any debts can be incurred. Thus, definite conditions precedent to the corporation's engaging in busi-

(1910). Cf. *Farmer's Loan & Mortg. Co. v. Langley*, 166 La. 251, 117 So. 137 (1928), where the court found the evidence as to alleged fraudulent misrepresentations insufficient, that the stockholders had been guilty of laches and that the fraud had been waived.

38. La. Act 250 of 1928, § 6, III [Dart's Stats. (1939) § 1086, III].

39. This provision is not found in corresponding Section 6 of the Uniform Business Corporation Act, 9 U.L.A. 49 (Perm. ed. 1932). It has been described by one writer as "rather harsh." Rutledge, *Significant Trends in Modern Incorporation Statutes* (1937) 22 Wash. L. Rev. 305, 317.

40. La. Act 250 of 1928, § 22 [Dart's Stats. (1939) § 1102].

41. La. Act 180 of 1910, § 15 [Dart's Stats. (1939) § 1194].

42. La. Act 50 of 1928, § 16 [Dart's Stats. (1939) § 1096]. See page 616. *infra*, for a full discussion of this section.

43. 150 So. 421 (La. App. 1933).

44. Art. 275(7), La. Code of Practice.

ness operations (as distinguished from the inception of corporate existence) are set out in the Louisiana statute. Section 8⁴⁵ specifies \$1,000 as the minimum amount of capital with which business may be begun. Then too, the articles must state the amount of paid-in capital with which the corporation will begin business;⁴⁶ and Section 9⁴⁷ expressly makes the payment of this amount a further condition precedent to the beginning of corporate business operations. Teeth are put in this provision by the imposition of liability upon the participating officers and upon the directors not dissenting, for the transaction of business in violation thereof.⁴⁸

THE DE FACTO PROBLEM

The general rule, that there can be no de facto corporation until the articles of incorporation have been filed or recorded as required by law,⁴⁹ was incorporated in the Uniform Act. It provides that where the corporation begins business and incurs debts before the articles have been filed, the participating officers and directors shall be personally liable.⁵⁰ No liability is imposed on the shareholders. Interpreting a provision of this type, the Washington Supreme Court has held that a corporation is not bound by a contract entered into by its directors before the articles were filed.⁵¹

The fundamental idea that corporate existence shall begin upon the filing or recording of the articles is definitely stated in Section 5 of the Louisiana Act, and Section 9, I(a) provides that

45. La. Act 250 of 1928, § 8 [Dart's Stats. (1939) § 1088]. For a collection of other statutes with similar minimum requirements, see Rutledge, *supra* note 39, at 334, n. 129.

46. La. Act 250 of 1928, § 3, I(g) [Dart's Stats. (1939) § 1082, I(g)].

47. *Id.* at § 9, I(b) [Dart's Stats. (1939) § 1089, I(b)].

48. *Id.* at § 9, II [Dart's Stats. (1939) § 1089, II]. The officers and assenting directors are liable jointly and severally with the corporation and each other.

49. 8 Fletcher, Corporations, 129, § 3820. Among the cases cited is *Provident Bk. & Trust Co. v. Saxon*, 116 La. 408, 40 So. 778 (1906), holding that a recording of the charter was necessary for a de facto corporation under La. Act 120 of 1904, § 1 [Dart's Stats. (1939) § 1155]. Accord: *Spencer Field & Co. v. Cooks*, 16 La. Ann. 153 (1861).

50. Uniform Business Corporation Act, § 8, II, 9 U.L.A. 51 (Perm. ed. 1932).

51. *Mootz v. Spokane Racing and Fair Ass'n*, 189 Wash. 225, 228-229, 64 P. (2d) 516, 518, Main, J., declared: "Section 5, chapter 185, page 776, Laws 1933, after providing for the filing of the articles of incorporation with the secretary of state, provides that, upon the issue of the certificate of incorporation by that officer, 'the corporate existence shall begin.' No authority has been cited, and we know of none, which holds that there can be a de facto corporation prior to the time that the articles of incorporation are filed with the proper officer."

the corporation shall not begin business until the articles have been filed for record. In subsection II of Section 9, however, the drafters departed from the wording of the Uniform Act. That subsection expressly provides for liability of the corporation, jointly and severally with its participating officers and non-dissenting directors, in all cases where business is prematurely begun. Following the express mandate of this provision, the Louisiana court has held that the officers, directors, and the corporation were jointly and severally liable for a debt incurred prior to the recording of the articles of incorporation.⁵² Reading Sections 5 and 9, II, together, we have a situation of corporate liability based upon a transaction which occurred before the corporation came into existence. This anomalous result would have been avoided by consistently following the wording of the Uniform Act, which treats the filing of the articles as the point at which, for all purposes, corporate existence shall begin.

Section 10⁵³ provides that the certificate of incorporation, issued by the Secretary of State, shall be conclusive evidence of proper incorporation as against all but the State. This section establishes the definite, easily interpreted rule that once the certificate is issued, no private party can set up defects in organization and collaterally attack the corporate existence. It thus clears away some of the uncertainties and ambiguities of the *de facto* doctrine.⁵⁴ It should be noted, however, that where the State is involved, as in forfeiture proceedings, the certificate is only *prima facie* evidence of due incorporation.

CONSTRUCTIVE NOTICE DOCTRINE REJECTED

There is an erroneous idea, sometimes entertained by courts, that persons dealing with a corporation are charged with constructive notice of the contents of the articles of incorporation

52. *Avoyelles Wholesale Grocery Co. v. Ville Platte S. Co.*, 17 La. App. 56, 135 So. 251 (1931).

53. La. Act 250 of 1928, § 10 [Dart's Stats. (1939) § 1090]. This section supersedes La. Act 120 of 1904, § 1 [Dart's Stats. (1939) § 1155], which established the requirements of a *de facto* corporation.

54. 9 U.L.A. 52 (Perm. ed. 1932). The commissioners declare, "The object of this section [Section 9 of Uniform Business Corporation Act] is to solve the *de facto* problem." See also Levin, *Blind Spots in the Present Wisconsin General Corporation Statutes* (1939) Wis. L. Rev. 173, 181, where the writer states, "The purpose of such a provision is obvious. Under it, there would be no corporation *de facto*, by estoppel or otherwise, until the certificate of incorporation has been issued. After the certificate has once been issued, no attack could be made on the corporate existence, except in an action of *quo warranto* brought by the state to challenge the assumption by individuals of corporate powers."

and other documents filed and recorded pursuant to law. Such notice has occasionally been assigned as a reason for treating the individual dealing with the corporation as *particeps criminis* and denying recovery upon a partially executed ultra vires contract. Section 11⁵⁵ removes this confusing element from the field of ultra vires transactions, by expressly declaring the generally accepted view that the reason for requiring the articles of incorporation and certain other documents to be filed is that all persons may be afforded an opportunity to ascertain the contents of such papers. The purpose is not to charge persons dealing with a corporation with constructive notice of such documents and the contents thereof,⁵⁶ as is true in the case of land registration certificates.

CORPORATE CAPACITY AND AUTHORITY

The concept of limited corporate capacity has been another source of difficulty and conflict in the ultra vires cases. Some courts, reasoning from the false premise that a corporation cannot do what it has no authority to do, have held that no performance on either side can give any validity to, or be the foundation of, any right of action upon an ultra vires contract.⁵⁷ Section 12, subsection I,⁵⁸ directly repudiates this doctrine by stating a clear-cut distinction between corporate *capacity* and *authority*. The section declares that a corporation shall have the inherent capacity of natural persons, but its authority is limited to the doing of such acts "as are necessary or proper to accomplish its purposes as expressed or implied in the articles or may be incidental thereto."⁵⁹

55. La. Act 250 of 1928, § 11 [Dart's Stats. (1939) § 1091]. A similar provision in the Michigan Corporation Act makes an exception in the case of shareholders, officers and directors and charges them with knowledge of the contents of the articles. Mich. Pub. Act 327 of 1931, § 9.

56. For a fine discussion and criticism of the "constructive notice" doctrine, see Stevens, A Proposal as to the Codification and Restatement of the Ultra Vires Doctrine, 36 Yale L. J. 297, 326 (1927), where it is suggested that an express provision, such as Section 11, should be adopted. See also 10 Corn. L. Q. 498 (1925); 9 U.L.A. 55 (Perm. ed. 1932). Commissioners' Notes to corresponding Section 10 of the Uniform Business Corporation Act.

57. Central Transportation Co. v. Pullman Car Co., 139 U.S. 24, 11 S.Ct. 478, 35 L. Ed. 55 (1891).

58. La. Act 250 of 1928, § 12, I [Dart's Stats. (1939) § 1092, I]. See 9 U.L.A. 57-62 (Perm. ed. 1932) for discussion of similar provisions in the Uniform Business Corporation Act.

59. For a discussion of implied and incidental powers see State v. New Orleans Warehouse Co., 109 La. 64, 33 So. 81 (1902), where it was held that a railroad company might lease the second floor of its depot building to a warehouse company since: (1) it could not be expected to allow the upper floor to be idle, and (2) the presence of a warehouse at the station would promote the convenience of shipping and so could be classed as fairly incidental to the railway business.

This is in line with the majority view of our state courts: that the corporation's *ultra vires* acts are unauthorized only,⁶⁰ and may under certain circumstances give rise to corporate liability.

Professor Ballantine has criticized a similar provision for its failure to go further and point out the specific consequences of unauthorized action.⁶¹ The drafters of the Uniform Business Corporation Act considered this possibility, but wisely concluded that the many varying factors involved made it unwise to adopt a rigid statutory rule as to when collateral attack upon the corporate authority should be permitted.⁶² Section 12 is declaratory of the majority state view, as to the nature and effects of *ultra vires* acts, and ample authority for its construction is furnished by the decided cases. Little doubt exists as to the right of a stockholder to enjoin *ultra vires* action,⁶³ as to the liability of a corporation for torts committed in the course of an *ultra vires* transaction,⁶⁴ or as to rights acquired under fully performed *ultra vires* contracts.⁶⁵ At the other extreme is the purely executory contract, which will and should be held unenforceable; for the right of the shareholder to insist that corporate resources shall be used only for the purposes stated in the articles, or incidental thereto, is more important than the right of third persons to insist upon

60. *Bissel v. Michigan S. & N. R.R.*, 22 N.Y. 258 (1860).

61. Ballantine, A Critical Survey of the Illinois Business Corporation Act (1934) U. of Chi. L. Rev. 357, 381-383; Ballantine, Questions of Policy in Drafting a Modern Corporation Law (1931) 19 Calif. L. Rev. 465, 473-475.

62. "The variety of the circumstances from which ratification, estoppel, negligence or laches may be inferred is so infinite that it would be unwise to attempt to formulate a statutory rule to control the decisions upon this aspect of the *ultra vires* problem. The principles now exist in the common law and are being satisfactorily applied to cases of *ultra vires* corporate action." Commissioners' Notes to the Uniform Business Corporation Act, 9 U.L.A. 61 (Perm. ed. 1932).

For an interesting and novel discussion of the *ultra vires* problem, see Stone, *Ultra Vires and Original Sin* (1940) 14 Tulane L. Rev. 190, with a complete bibliography of other writings at 199, n. 28.

63. The shareholder can enjoin *ultra vires* action, even though advantageous. *Coleman v. Eastern Counties Ry. Co.*, 10 Beav. 1 (1846). The right to question and enjoin *ultra vires* action is limited to the State or someone (as a shareholder) directly interested in the corporation. *Nelson v. Texas & Pacific Ry.*, 152 La. 117, 92 So. 754 (1922).

64. *Chamberlain v. Southern California Edison Co.*, 167 Cal. 500, 140 Pac. 25 (1914).

65. Where a contract has been fully performed on both sides, neither party can get it set aside and recover the consideration paid. *Reimann v. New Orleans Public Service, Inc.*, 191 La. 1079, 187 So. 30 (1939), discussed with citation of other authorities, *Work of the Louisiana Supreme Court* (1939) 2 LOUISIANA LAW REVIEW 31, 128.

Also, a party who has received full performance is estopped to raise the defense of *ultra vires* to an action on the contract. *Bath Gas Light Co. v. Claffy*, 151 N.Y. 24, 45 N.E. 390 (1896).

performance of such contracts.⁶⁶ There will still be a somewhat nebulous zone occupied by the partially executed *ultra vires* agreement.

Although Section 12, I, broadly declares that the corporation "shall have the capacity to act possessed by natural persons," our courts will probably continue to apply the general rule that a corporation has no power to enter into a partnership, unless the authority is expressly conferred.⁶⁷ This rule is bottomed on the fundamental policy that the corporation should act through its board of directors. The partnership arrangement, where each member binds the firm when acting within the scope of the undertaking, involves too great a delegation of the powers of management. The Louisiana Act embodies the principle of director management,⁶⁸ and the broad statement of Section 12, I, may well be interpreted in the light of that concept. Of course, joint ventures and other arrangements analogous to the partnership, but where there is no yielding of the corporate management, will be considered *intra vires*.⁶⁹

Subsection II of Section 12 specifically enumerates a number of things that a corporation is authorized to do. This subsection is prefaced by the important qualification, "Without limiting or enlarging the grant of authority contained in subdivision I." Thus, all such authorizations are subject to the general limitation that the acts done must be in furtherance of or incidental to the corporate purpose. Also, the enumeration is not exclusive, and acts not included therein may come within the general grant of authority set out in subsection I. The specific provisions of subsection II, however, will prove very valuable—indicating the general types of permissible corporate activity and clearing up a few uncertainties in the common law.⁷⁰

66. See Rutledge, *supra* note 39, at 319, 320, for an analysis of the California statute, presumably drafted by Professor Ballantine, which abolishes the defense of *ultra vires* as between the corporation and third parties or shareholders.

67. *Mallory v. Hananer Oil-Works*, 86 Tenn. 598, 8 S.W. 396 (1888); 6 *Fletcher, Corporations*, 243, § 2520. However, where the partnership arrangement has been in operation and losses suffered, the individual partner is estopped to set up the *ultra vires* nature of the contract in an effort to escape his share of the losses. *J. P. Barnett Co. v. Ludeau*, 171 La. 21, 129 So. 655 (1930).

68. Act 250 of 1928, § 34, I [*Dart's Stats.* (1939) § 1114, I].

69. *L. J. Mestier & Co. v. Chevalier Pavement Co.*, 108 La. 562, 568, 32 So. 520, 522 (1901); *Nicholls, C. J.*, declared: "True, this corporation could not be a member of a partnership. It had no such power, yet it could bind itself to the extent of dividing profits as a consideration for advances made, as we understand was done in this case." For further authority see 6 *Fletcher, Corporations*, 245, 247, § 2520.

70. Compare the less comprehensive provision of the Uniform Business

Clauses (c) and (f) of Section 12, II, recognize the fundamental rights of a corporation to sue or be sued in the corporate name, and to transact corporate business. It has been held that non-payment of its annual franchise tax does not preclude a domestic corporation from bringing suit or from continuing to conduct business in the state.⁷¹

Clause (e) clears up any doubt that may have existed as to the authority of a corporation to subscribe for or purchase shares of stock in another corporation. When read in connection with the limitation in subsection I, it may be regarded as merely a codification of the general common law rule that a corporation may purchase stock in furtherance of its corporate purposes, express, incidental, and implied.⁷² This clause, thus construed, does not permit a corporation to engage indirectly in ultra vires activity through the ownership of stock in other corporations having dissimilar purposes, but does recognize the right of a corporation to carry on its authorized business by means of subsidiary corporations. The corporation is given the full right to vote the shares purchased, and thus may exercise a legitimate control of its subsidiaries.⁷³ Also the suggestion has been made that "the taking of stock as security for or in payment of a debt, and the investment of idle funds in the stock or securities of other corporations would be in furtherance of its corporate purposes."⁷⁴

Corporation Act, § 11, II, 9 U.L.A. 56 (Perm. ed. 1932). Clauses e, g, h, i, j, and k of the Louisiana Act, § 12, II, are not found in the Uniform Act.

71. *Shreveport Long Leaf Lumber Co. v. Jones*, 188 La. 519, 177 So. 593 (1937), applying Section 12, II(c), (f), of the Louisiana Business Corporation Act. *Odom, J.*, held (188 La. 519, 526, 177 So. 593, 595) that the statute levying an annual franchise tax on domestic corporations did not state or intimate "that the payment of the tax is a condition precedent to the corporation's engaging or continuing to engage in business," but was "a revenue act pure and simple." *Accord: Natchitoches Finance Co. v. Smith*, 175 So. 915 (La. App. 1937).

A different result has been reached as to foreign corporations "doing business in this state." They are precluded by La. Act 8 of 1935 (3 E. S.) [Dart's Stats. (1939) § 1247.1] from bringing suit unless all taxes and licenses are paid. *R. J. Brown Co. v. Grosjean*, 189 La. 778, 180 So. 634 (1938), discussed, *Work of the Louisiana Supreme Court (1939)* 1 LOUISIANA LAW REVIEW 314, 406.

72. Professor Ballantine, after summarizing the general state of the common law authorities, concludes, "It would seem wise to give a corporation express power to hold stock in other corporations and not trust to the implication of such power where it may be incidental to the general objects." Ballantine, *Private Corporations* (1927) 221.

73. Under La. Act 267 of 1914, § 7(j), a corporation could not vote over 10% of the capital stock in another corporation.

74. Commissioners' Notes to Section 12 of Uniform Business Corporation Act, 9 U.L.A. 63 (Perm. ed. 1932).

Clause (h) authorizes the corporation to borrow money and to issue bonds, notes, or other evidences of indebtedness, and to secure the same by a mortgage, pledge or hypothecation of any kind of corporate property. There is no limitation upon the amount of indebtedness that may be incurred, nor is the consent of the shareholders necessary to authorize long term indebtednesses. The absence of such restrictions in the Louisiana Act and in other modern corporation statutes has been mildly criticized by one writer, who suggests that the total amount of corporate debts should bear some specific relation to the issued capital stock in order that "the corporate shoestring should not be too short."⁷⁵

Clause (j) grants authority to guarantee the shares, bonds, contracts and other obligations (including interest and dividends thereon) of other corporations, domestic and foreign. Out of abundant caution, the drafters of the Act expressly stipulated that this authority to guarantee obligations of other corporations could be exercised only "to accomplish its purposes as stated in the articles." This restrictive clause is unnecessary, since all enumerations of authority contained in subsection II are subject to the corporate purpose limitation of subsection I. The provision does, however, indicate a clear intention that the clause should be regarded merely as a codification of the general rule that a corporation may bind itself as surety or guarantor where there is a fairly clear and direct connection with the promotion of the authorized business of the corporation.⁷⁶ In *Cook v. Ruston Oil Mills & Fertilizer Co.*⁷⁷ the Louisiana Supreme Court held a hardware company liable as indemnitor of the surety on a contractor's bond. In overruling the defense of ultra vires, Justice Rogers stated the general proposition that a trading corporation may guarantee its customer's obligations, and pointed out that in the instant case the hardware company stood to benefit by the builder's contract through the sale of supplies and materials.

SHARES OF STOCK—CLASSIFICATION AND PREFERENCES

The proprietary interest in the corporation is represented by shares of stock. These shares, evidencing the undivided interest

75. Rutledge, *supra* note 39, at 323.

76. 6 Fletcher, *Corporations*, 379, § 2591.

77. 170 La. 10, 127 So. 347 (1930), the court also used the familiar "estoppel" argument. The earlier case of *Robert Gair Co. v. Columbia Rice Packing Co.*, 124 La. 193, 50 So. 8 (1909), was virtually overruled, but was distinguished on the ground that the benefit to the guaranteeing corporation was not so direct and clear as in the case at bar.

of the owner or "shareholder," may be divided into classes with or without par value, and with such preferences, rights, or restrictions as are provided for in the articles. Section 13⁷⁸ deals with the classification and designations of shares, and subsection III is significant. It declares the general rule that, "Except as otherwise provided in the articles and referred to in the certificate of stock, each share shall be in all respects equal to every other share."

Where the articles are not fully explicit, we must look to the case law to determine the extent of the "preferred" shareholder's rights, always bearing in mind that he has only those preferences which are expressly stated or may be reasonably implied from his contract. For example, stock with a preference as to dividends is not entitled to priority in the distribution of assets on dissolution, unless such right is expressly stipulated in the articles.

There is still considerable conflict as to whether shareholders with a preferential dividend right are, when the corporate venture proves very profitable, entitled to an additional share in the surplus available for dividend distribution. The preferred shareholder is given a security of income return not enjoyed by shareholders of the common variety. If the enterprise meets with only indifferent success, the preferred shareholder may receive dividends, while the common shareholder gets nothing. It is logical to conclude that the security of the preferential rate was accepted in lieu of equal participation in profits. Thus, the better view, probably representing the weight of authority, is that the preferred shareholder should receive only the stipulated dividend, with the entire balance being distributed among the common shareholders.⁷⁹ Other courts have held that after the common shareholders have been paid a dividend equal to the preferential dividend, the preferred shareholders are entitled to share equally with the common shareholders in any further profits available for dividends.⁸⁰ No Louisiana decisions on this point have been found. If the incorporators desire that the common shareholders, who assume the greater risk, should get the extra profits if the business is exceptionally successful, they should make this definite, and expressly stipulate that the preferred shareholder shall get a cer-

78. La. Act 250 of 1928, § 13 [Dart's Stats. (1939) § 1093].

79. Powers Foundry Co. v. Miller, 166 Md. 590, 171 Atl. 842 (1934); Niles v. Ludlow Valve Mfg. Co., 202 Fed. 141 (C.C.A. 2d, 1913), affirming 196 Fed. 994 (1912); Will v. United Lankat Plantation Co., 1914 A.C. 11, 83 L.J. Ch. (N.S.) 195, 109 L.T. (N.S.) 754 (1914). For a full review and discussion of decisions in point, see Note (1921) 19 Mich. L. Rev. 463-486.

80. Sternbergh v. Brock, 225 Pa. 279, 74 Atl. 166 (1909).

tain percentage "and no more."⁸¹ Conversely, they should specifically state that the preferred shareholders are to share equally in additional profits, if such is their intention.

SHARE CERTIFICATES

The certificate of stock is *prima facie* evidence both of the validity of the issue of stock and of the ownership of the person named therein.⁸² Section 21⁸³ was inserted to dovetail the Business Corporation Act into, and to focus attention upon, the Uniform Stock Transfer Act, which was adopted by Louisiana in 1910.⁸⁴ Under this statute a transfer of the certificate, properly indorsed, operates as a transfer of the shares of stock to a bona fide purchaser. By it the share of stock is given full attributes of negotiability, and the certificate, when indorsed in blank by the owner, passes freely from hand to hand in the same manner as a check similarly indorsed.⁸⁵ A share of stock may change hands several times, merely on the blank indorsement of the registered owner, until eventually a holder decides to have the old certificate cancelled and a new one issued in his name. In the meantime, the corporation, in the absence of notice to the contrary, may safely rely on its books and allow voting rights or send dividend checks to the registered owner.⁸⁶

The form and contents of the certificate is set out in Section 14.⁸⁷ Subsection II declares what must be stated in the certificate

81. *Tennant v. Epstein*, 356 Ill. 26, 189 N.E. 864 (1934), noted (1934) 83 U. of Pa. L. Rev. 91.

82. *Davidson v. American Paper Mfg. Co.*, 183 La. 69, 175 So. 753 (1937). La. Act 250 of 1928, § 1, VIII [Dart's Stats. (1939) § 1080, VIII].

Where a certificate of stock has been fraudulently issued to another, the true owner can secure a cancellation of such certificate and compel the issuance of a new certificate to him. *McWilliams v. Geddes & Moss Undertaking Co.*, 169 So. 894 (La. App. 1936). *McCaleb, J.* (169 So. 894, 896) quotes from *Succession of McGuire*, 151 La. 514, 520, 92 So. 40, 42 (1922), as follows: "From the foregoing it is very plain that a certificate of stock is merely a paper evidence created for convenience, of the ownership of the share of stock; . . . that the thing which is in reality the subject of ownership is the share of stock itself."

83. La. Act 250 of 1928, § 21 [Dart's Stats. (1939) § 1101].

84. La. Act 180 of 1910 [Dart's Stats. (1939) §§ 1180-1205]. Space does not permit a full discussion of the problems arising under this statute.

85. "The elements of negotiability lacking at the common law, have now been supplied by the Uniform Stock Transfer Act and a stock certificate indorsed in blank passes freely and becomes a 'courier without luggage whose countenance is its passport.'" Note (1939) 4 Univ. of Newark L.R. 220, 221. See also Note (1939) 37 Mich. L. Rev. 480.

86. For a complete discussion of problems arising out of the negotiability of the stock certificate, see Dewey, *Transfer Agent's Dilemma—Conflicting Claims to Share of Stock* (1939) 52 Harv. L. Rev. 553.

87. La. Act 250 of 1928, § 14 [Dart's Stats. (1939) § 1094]. The certificate

and should be carefully complied with. Where shares of more than one class are authorized, the certificate must recite "the rights, voting powers, preferences and restrictions granted to or imposed upon the shares of each class, or a reference to the articles relating thereto." This enables the shareholder to acquire easily an adequate idea of the relative position of his stock in the corporate structure. Subsection III follows the general practice of prohibiting the expression of any nominal or par value on certificates for no-par stock.⁸⁸ However, the certificate may state a fixed amount at which these shares may be redeemed, or it may contain such statements as may be desired concerning the shareholder's interest in the event of dissolution. It is believed that such statements are "no indication or false representation as to what has been paid to the corporation upon those shares."⁸⁹

ALLOTMENT AND CONSIDERATION FOR SHARES

A subscriber does not become a shareholder until allotment of shares to him, usually by the board of directors in response to the application contained in his subscription.⁹⁰ An exception is made in the case of pre-incorporation subscriptions, which are automatically accepted, and the subscriber becomes a shareholder coincident with incorporation.⁹¹

While Section 15 provides that subscriptions for shares may be made payable with cash, property, or services,⁹² it expressly prohibits the issuance of shares having a par value at less than the full par value in cash or other property fairly valued.⁹³ This does not prevent the issuance of shares to an underwriter at less than par. The underwriter's discount is really a commission, and

must be signed by the president and secretary, or by such other officers of the corporation as the articles or by-laws may provide. *Id.* at subsection I.

88. The spirit of the provision "is to eliminate misrepresentation arising from a difference between a value appearing upon the face of the certificate and the actual value of the divisional interest in corporate assets to which the certificate represents the holder to be entitled." Commissioners' Notes to a substantially identical prohibition in Section 14 of the Uniform Business Corporation Act, 9 U.L.A. 65 (Perm. ed. 1932).

89. Commissioners' Notes, 9 U.L.A. 65 (Perm. ed. 1932).

90. See La. Act 250 of 1928, § 1, IX [Dart's Stats. (1939) § 1080, IX]. The word "allot" was adopted (Section 1, IX) to express the act of the corporation in accepting the subscriber's subscription and making him a shareholder. When the shares are paid for the certificate is "issued." Commissioners' Notes to the Uniform Corporation Act, 9 U.L.A. 69 (Perm. ed. 1932).

91. La. Act 250 of 1928, § 1, IX, and § 6, III [Dart's Stats. (1939) § 1080, IX, § 1086, III].

92. *Id.* at § 15, II [Dart's Stats. (1939) § 1095, II].

93. *Id.* at § 15, III [Dart's Stats. (1939) § 1095, III].

may constitute a reasonable compensation (expressly authorized in Section 7) for the risk taken in underwriting a bloc of stock.⁹⁴

The character and value of consideration to be paid for no-par stock is to be determined by the incorporators where the subscription is signed before incorporation. The character and value of the consideration for subsequent allotments is to be determined by the shareholders, unless such authority is specially conferred on the board of directors by the shareholders or the articles.⁹⁵ Thus, unless the power is delegated to the directors, new members cannot come into the enterprise, except by contributing such sums or value as the existing shareholders determine is a fair consideration for the participating rights in assets and profits which they will acquire.

Par value shares are sometimes sold at a premium. The conflict at common law⁹⁶ as to how such premiums should be treated has been removed by the Louisiana Act. Only the par value is to be considered as "capital stock,"⁹⁷ and the remainder is paid in "surplus,"⁹⁸ out of which dividends may be paid.⁹⁹

Ordinarily sound financing does not permit the treatment of any part of the consideration received for no-par shares as paid-in *surplus*. Such procedure would make any consideration so received available for the payment of unearned dividends. In certain cases, however, this practice may be desirable. For instance, in the reorganization of a corporation having a surplus, it is necessary to tag and set aside that surplus. Otherwise, the common stock of the new corporation will automatically soak it up in the capital account and make it unavailable for dividend purposes.¹⁰⁰

94. *Id.* at § 7 [Dart's Stats. (1939) § 1087] provides that "A corporation may . . . pay or allow reasonable compensation for the sale or underwriting at the time of organization or thereafter of its shares, or any part thereof." See also *In re Licensed Victuallers Mutual Trading Ass'n*, 42 Ch. 1 (C.A. 1899).

95. La. Act 250 of 1928, § 15, IV [Dart's Stats. (1939) § 1095, IV]. For a comprehensive recent discussion of the problem of consideration for no-par shares, see Masterson, *Consideration for Non-Par Shares and Liability of Subscribers and Stockholders* (1939) 17 Tex. L. Rev. 247.

96. There was a conflict in the decisions. Some courts held that where par value stock sold at a premium, the entire amount received must be considered as "capital stock" and was thus unavailable for dividends. *Merchants' & Insurers' Reporting Co. v. Youtz*, 39 Cal. App. 226, 178 Pac. 540 (1918). Others held that such premiums should be treated as paid-in surplus from which dividends may be paid. *Equitable Life Assur. Society v. Union Pacific R.R.*, 212 N.Y. 360, 106 N.E. 92 (1914).

97. La. Act 250 of 1928, § 1, X(a) [Dart's Stats. (1939) § 1080, X(a)].

98. *Id.* at § 1, XIII [Dart's Stats. (1939) § 1080, XIII].

99. *Id.* at § 26, II [Dart's Stats. (1939) § 1106, II].

100. See Berle, *Problems of Non-Par Stock* (1925) 25 Col. L. Rev. 43, 49.

Section 25¹⁰¹ authorizes those charged with the valuation of consideration received for no-par shares to "at that time specify" an amount of such value that is to be treated as surplus. This broad grant of authority may be abused by promoters intending to buoy the faith of investors through the subsequent payment of unearned dividends.

Section 16, subsection I,¹⁰² following an express mandate of the Louisiana Constitution,¹⁰³ prohibits the issuance of a certificate of stock "until the shares represented thereby have been fully paid for." Thus, the share certificate cannot be issued in payment for services yet to be rendered, or property yet to be received.¹⁰⁴ This restriction is necessitated by the negotiable qualities of the certificate. It does not prevent a subscriber from immediately becoming a shareholder upon the allotment of his shares, but does prohibit the issuance of a certificate to him until the shares are fully paid for.¹⁰⁵ Subsection II eliminates any possible uncertainties as to the effect of payment by promissory note or check. Adopting the Louisiana rule¹⁰⁶ (which is generally regarded as the preferable one)¹⁰⁷ this subsection specifically states that shares allotted upon receipt of a shareholder's note or uncertified check "shall not be considered as fully paid for until such note or check has been paid."

The shareholder who honestly fulfills the terms of his subscription is accorded full protection against any further liability

101. La. Act 250 of 1928, § 25 [Dart's Stats. (1939) § 1105]. A substantially identical provision is found in the Uniform Business Corporation Act, § 23, 9 U.L.A. 74 (Perm. ed. 1932).

102. La. Act 250 of 1928, § 16, I [Dart's Stats. (1939) § 1096, I].

103. La. Const. of 1921, Art. XIII, § 2, provides, "Corporations shall not issue stock or bonds except for labor done, or money or property actually received; and all fictitious issues of stock shall be void; and any corporation issuing such fictitious stock shall forfeit its charter."

104. In refusing specific performance of a contract by which a corporation was to issue shares in payment for services yet to be rendered, the Louisiana Supreme Court declared, "'Labor done or money or property actually received,' cannot possibly mean labor to be done or money or property to be received." *Lothrop v. Goudeau*, 142 La. 342, 354, 76 So. 794, 798 (1917).

105. Shares are often allotted with the shareholder only paying \$50.00 (or some such amount) on each \$100.00 par value share. The certificates of stock are not issued and no attempt is made to represent the shares as fully paid. The subscriber becomes a stockholder with the remaining \$50.00 to be paid upon a call by the board of directors, which may never be made if the corporation does not need the additional money. Of course, if the corporation runs into financial difficulties, the shareholder can be compelled to pay the balance, so far as necessary to meet corporate debts.

106. *State v. New Orleans Debenture Redemption Co.*, 51 La. Ann. 1827, 26 So. 586 (1899), holding that the giving of a promissory note was not a sufficient compliance with a statutory requirement of "payment in cash."

107. 11 Fletcher, Corporations, 447, § 5195.

to the corporation. Section 16, subsection III declares that his shares shall be "fully paid" and "non-assessable." Section 17¹⁰⁸ provides that, for the purpose of determining whether shares have been fully paid for, the valuation placed upon consideration other than cash by the incorporators, shareholders or directors, as the case may be, shall be conclusive. Section 19, subsection I¹⁰⁹ states that a shareholder who complies with the terms of his subscription shall be under no further liability to the corporation with regard to his shares.

Subsection II of Section 19 states the general rule that a shareholder is not personally liable for debts of the corporation.¹¹⁰ This, and the above provisions, might be interpreted as expressing a legislative intent that the shareholder who innocently takes shares for over-valued services or property is completely protected. There is, however, a serious doubt as to the constitutionality of so broad a grant of immunity.¹¹¹ Then too, Sections 17 and 19, I, specifically refer to liability "to the corporation," and it is consistent with a general policy of protecting corporate creditors that these words of the Act should be construed to mean what they say, and nothing more. Third persons dealing with a corporation have a right to expect that when stock has been issued as paid up, full value in money or property has gone into the corporate coffers.

Subsection III expressly preserves any rights which the corporation or any person may have because of fraud practiced by

108. La. Act 250 of 1928, § 17 [Dart's Stats. (1939) § 1097]. Also conclusive is Section 17(b) "the valuation placed by the board of directors upon the corporate assets in estimating the surplus to be transferred to capital as payment for shares to be allotted as stock dividends."

109. La. Act 250 of 1928, § 19, I [Dart's Stats. (1939) § 1099, I].

110. *Sutton v. Moreland*, 177 So. 396 (La. App. 1937) (shareholders are not personally liable on an agreement executed by them as agents for the corporation).

111. Such a provision must be construed in the light of Art. XIII, § 2, of the Louisiana Constitution of 1921, *supra* note 103. In *Rapides Grocery Co. v. Grant*, 165 La. 593, 599, 115 So. 791, 793-794 (1928), the Louisiana Supreme Court unqualifiedly declared that "under said article, the value of property or labor received in payment of a stock subscription must be equal to the face value of the shares, and the subscriber is liable to the creditors of the insolvent corporation for the difference between the value of the property given in payment and the par value of the shares." *Accord: Webre v. Christ*, 130 La. 450, 58 So. 145, (1912). *Cf. Walmsley v. Brothers*, 152 La. 148, 92 So. 766 (1922), where the court refused to hold a shareholder liable to the receiver of a failing corporation for the difference between the rather nominal actual value of services rendered and the par value of stock received. *O'Niell, J.*, emphasized the facts that no bad faith was shown, and that there was no affirmative showing that credit had been extended on the strength of any one's faith in the ostensible paid-in capital.

an incorporator, director, officer or shareholder. Both creditors and the corporation have a clear cause of action against the shareholder who knowingly participated in a stock-watering scheme by paying for his shares with property at an over-valuation.¹¹²

In cases of gross over-valuation of property or services taken in payment for shares, Section 20 declares¹¹³ that the incorporators, shareholders, or directors (depending upon which is charged with the duty of evaluation) who knowingly or without reasonable care and inquiry, consented to or voted in favor thereof shall be jointly and severally liable¹¹⁴ to the corporation, for the benefit of shareholders and creditors. A shareholder, director or incorporator who was present at the meeting where the evaluation was made is presumed to have consented thereto, unless his dissent was promptly filed in the registered office of the corporation.¹¹⁵

In many instances a large part of a corporation's capital is secured through the sale of no-par stock. Often shares are issued for consideration other than cash. It is therefore important that prospective investors and creditors should be able to obtain full and accurate information upon which to determine a corporation's financial status. This is the basic policy behind the requirement in Section 18¹¹⁶ that a full and verified report of the share structure and the consideration received for shares must be filed with the Recorder of Mortgages and the Secretary of State within ninety days after incorporation. This report must include a descriptive statement of the amount and designations of the various classes

112. In *Dilzell Engineering & Constr. Co. v. Lehmann*, 120 La. 273, 45 So. 138 (1907), the defendants, managing the affairs of a corporation, had distributed stock with a face value of \$30,100.00 among themselves, and had given in return a worthless lease acquired by one of their number for about \$600.00. They were held liable to corporate creditors for the difference between the value of the property transferred and the face value of the shares received. Provosty, J., relied on Art. 13, § 2, of the Louisiana Constitution of 1921 (Art. 266 of La. Const. of 1898) and declared, "While it is not here said expressly that the value of the labor or property received in payment of the stock must be equal to the face value of the stock, that is the idea meant to be conveyed." (120 La. 273, 284, 45 So. 138, 142).

113. La. Act 250 of 1928, § 20, II [Dart's Stats. (1939) § 1100, II]. Subsection I provides joint and several liability for any incorporator, officer, or director who knowingly or negligently consents to or participates in an unlawful allotment of shares, the illegal issuance of a stock certificate, the making of a false statement in any document, or the omission to file any required statement or document.

114. The corporation need not sue *all* those charged with liability, and it may not be worth while to join those without liable assets. Joint and several liability is one and the same thing as liability in *solido*. *Garland v. Coreil*, 17 La. App. 17, 134 So. 297 (1931).

115. La. Act 250 of 1928, § 20, III [Dart's Stats. (1939) § 1100, III].

116. *Id.* at § 18 [Dart's Stats. (1939) § 1098].

of shares which may be issued, and which actually have been allotted. It must state the amount of cash, or a fair general description and the value placed on consideration other than cash, which was received in payment for shares allotted. Supplemental reports must be filed after each subsequent allotment of shares not payable in cash, or of those payable in cash at a different price from shares previously sold. In addition to the joint and several liability of corporate officers to anyone suffering a loss because of their failure to file the required report,¹¹⁷ the section imposes a fine, not exceeding \$500, on the corporation.¹¹⁸

POWER OF CORPORATION TO REPURCHASE SHARES AND TO ISSUE CONVERTIBLE SECURITIES

Section 23 adopts the prevailing rule that a corporation may purchase its own shares "only out of surplus available for dividends."¹¹⁹ This limitation on the power to repurchase is postulated on the idea that the capital stock is in the nature of a "trust fund" for the security of creditors, and represents money or property actually and permanently devoted to the corporate enterprise. The exercise of an unlimited power to repurchase might effect a serious impairment of the actual working capital of the corporation, with a consequent reduction of the creditor's margin of security. This follows through to the proverbially absurd, yet nevertheless possible, conclusion that if a corporation without any surplus repurchased most of its stock, the actual capital investment would vanish, and its treasury would be filled with cancelled certificates.¹²⁰

Except in certain specified instances, stock repurchases must be authorized by a two-thirds vote of each class of shares outstanding.¹²¹ Shares thus acquired become "treasury shares" until

117. *Id.* at § 20, I [Dart's Stats. (1939) § 1110, I]. See note 113, *supra*.

118. *Id.* at § 18, IV [Dart's Stats. (1939) § 1098, IV].

119. For a fine collection of statutes and cases in accord, see Comment (1938) 27 *Geo. L. J.* 217, 220-223. California and Illinois go even further and restrict such purchases to *earned* surplus. Cal. Civ. Code (Deering, 1931) § 347; Ill. Rev. Stat. Ann. (Smith-Hurd, 1935) c. 32, § 157.58.

Where there is an agreement by a corporation to purchase its own shares, with payment deferred, the financial condition of the corporation at the time of payment is controlling. *Robinson v. Wangemann*, 75 F. (2d) 756 (C.C.A. 5th, 1935); *In re Fechheimer Fishel Co.*, 212 Fed. 357 (C.C.A. 2d, 1914).

120. For a good criticism and discussion of the results of giving a corporation unlimited authority to repurchase its shares, see Nussbaum, *Acquisition by a Corporation of Its Own Stock* (1935) 35 *Col. L. Rev.* 971; Rutledge, *supra* note 39 at 322, n. 72, collects a number of other authorities adopting a similar view.

121. La. Act 250 of 1928, § 23, I(e) [Dart's Stats. (1939) § 1103, I(e)]. Such authority by shareholder vote is not required where the articles provide for

disposed of by sale or formal reduction of the capital stock.¹²² Unless the articles require cancellation, these treasury shares may be reissued and sold for such consideration as the board of directors may fix, but not for less than the price at which they were purchased.¹²³ If it is desired to cancel the purchased shares, the procedure for reduction of capital stock, set forth in Section 45, subsection IX, must be followed.¹²⁴ The necessity of a strict and prompt compliance with the requirements of Section 45, where a reduction of the corporation's capital stock is intended, was forcibly illustrated by the recent case of *State v. Stewart Brothers Cotton Co., Inc.*¹²⁵ In that case a corporation repurchased a third of its outstanding shares, intending to cancel the same and reduce the capital stock accordingly. However, a formal amendment of the articles was not passed or filed until three years later. The Louisiana Supreme Court adopted the general view that treasury shares are "outstanding" for taxation purposes until they are formally retired, and held that the corporation must pay a franchise tax upon the repurchased shares for the three years prior to the amendment of the articles effecting their cancellation.

Section 24¹²⁶ broadly provides that a corporation shall have authority to issue stock or securities convertible into "shares of any class or classes." Thus, preferred stock may be issued which the holder may at his option convert into common stock. This provision does not authorize agreements for the conversion of stock into bonds. Such a conversion would decrease the capital stock of the corporation and lessen the security of corporate creditors, for bondholders are themselves creditors rather than permanent investors in the corporate business.¹²⁷ It does, however, authorize the issuance of bonds convertible into shares of

redemption of shares, when such purchase is in the good faith collection or compromise of a debt, when the purchase is for the purpose of resale or allotment to employees, or when it is pursuant to a repurchase agreement with employees. Id. at § 23, I(a)-(d) [Dart's Stats. (1939) § 1103 I(a)-(d)].

122. Id. at § 23, II [Dart's Stats. (1939) § 1103, II].

123. Id. at § 23, III [Dart's Stats. (1939) § 1103, III].

124. Opinions of Attorney General, 1932-34, p. 193.

125. 193 La. 16, 190 So. 317 (1939); Discussed, Work of Louisiana Supreme Court (1939) 2 LOUISIANA LAW REVIEW 31, 128.

126. La. Act 250 of 1928, § 24, I(a) [Dart's Stats. (1939) § 1104, I(a)]. For a discussion of conversion privileges, see 11 Fletcher, Corporations, 752, § 5306.

127. A Kentucky statute authorizing the issuance of preferred stock convertible into bonds has been interpreted in such a way that preferred shareholders exercising the privilege did not secure priority over or even equality with corporate creditors. In re Phoenix Hotel Co. of Lexington, 13 F. Supp. 229 (1935), affirmed 83 F. (2d) 724 (C.C.A. 6th, 1936).

stock.¹²⁸ Such a privilege often makes the bonds of a new corporation very attractive. While the future of the corporate venture is still uncertain, the purchaser may retain his more secure status of a bondholder; but if the corporation proves successful, he may choose to relinquish that security and receive the greater income of a shareholder. Subsection IV requires that where shares upon which conversion rights are granted have a par value the conversion must be on a basis of not less than the par value of such shares. This forestalls any attempts to sell stock below par through the device of issuing sub-par bonds convertible into stock at their par value.

The issuance of stock purchase warrants, a practice which has only recently come into frequent use, is also authorized by Section 24.¹²⁹ These warrants may be issued in connection with the sale of stock or bonds. They are transferable and give the holder an option, at such future time and at such a price as is stipulated, to purchase stock (usually common) in the corporation. Thus, the cautious investor, who buys bonds or preferred stock, secures the additional privilege of coming in as a common shareholder, if and when the corporate business becomes well established. There are definite drawbacks to the free issuance of such warrants. They naturally tend to retard the advance of the common stock in the open market. Then too, the option is normally exercised at a time when the corporation is in good shape and either does not need additional capital or else could secure it more advantageously by other means. The option warrant is essentially an emergency measure, to be used as an added inducement when the corporation is having difficulty in securing needed funds.

DIVIDENDS

It is axiomatic in sound corporate finance that the assets which represent the capital investment in the corporation should be used but not used up. This fundamental idea of keeping the capital investment intact is embodied in the general rule of Sec-

128. It is expressly provided that conversion rights may be granted in connection with the sale of "any stock and/or securities." For a full discussion of bonds convertible into stock and the interpretation of such conversion agreements, see 6 Fletcher, Corporations, 540, §§ 2692-2695.

129. La. Act 250 of 1928, § 24, I(b) [Dart's Stats. (1939) § 1103, I(b)]. The device was used in 1872 as a part of the financing of the Illinois Central Railroad, but "had its great vogue in the boom stock market years of 1925-1929, when the investing public was 'common stock conscious.'" 19 Fletcher, Corporations, 63, § 8907.

tion 26¹³⁰ that dividends may be paid only out of some form of actual surplus. Subsection I provides the formula—"No corporation shall pay dividends in cash or property, except from the surplus of the aggregate of its assets over the aggregate of its liabilities, plus the amount of its capital stock."¹³¹ Further, the payment of such dividends out of a surplus arising from any sort of unrealized profits or appreciation of assets is expressly prohibited.¹³² Cash or property dividends may be paid out of "paid-in surplus," but notice regarding the source must be given to the recipient shareholders.¹³³

Subsection III permits the payment of a stock dividend¹³⁴ out of a surplus including those unrealized profits and unrealized appreciation items which are excluded from consideration when cash dividends are involved. The declaration of stock dividends is subject to two significant limitations, set out in subsection V. Par value shares must not be issued unless a corresponding amount of surplus is transferred to capital, thus forestalling the possibility of a stock-watering dividend. Also, where shareholders of one class receive shares of another class as a dividend, such payment must be authorized by a majority vote of shareholders of the latter class, whose relative voting rights will be affected.

In computing the aggregate of the corporate assets for purposes of dividends, whether payable in cash or shares, proper allowance must be made for depreciation, depletion, and known losses of every character.¹³⁵ There are certain so-called "wasting assets" corporations, which, by their very nature, consume and exhaust their principal assets in normal operation. For example, the oil wells, coal mines, leases, or patents which may constitute the most valuable assets of oil, mining or manufacturing companies, have only a limited life. There has been some conflict as to whether such a corporation is subject to the general rule, and must set up a reserve to replace capital deficiencies before declaring dividends out of current profits.¹³⁶ Subsection VI of Section 26

130. La. Act 250 of 1928, § 26 [Dart's Stats. (1939) § 1106].

131. For definitions see id. at § 1 [Dart's Stats. (1939) § 1080] X (capital stock), XII (assets), XIII (surplus).

132. Id. at § 26, I(b) [Dart's Stats. (1939) § 1106, I(b)].

133. Id. at § 26, II [Dart's Stats. (1939) § 1106, II].

134. The taxability of stock dividends is discussed by James, *The Present Status of Stock Dividends under the Sixteenth Amendment* (1939) 6 U. of Chi. L. Rev. 215.

135. La. Act 250 of 1928, § 26, IV [Dart's Stats. (1939) § 1106, IV].

136. In *Wittenberg v. Federal Mining & Smelting Co.*, 15 Del. Ch. 147, 133 Atl. 48 (1926), the court enjoined payment of dividends on common stock without setting up a "wasting assets" reserve to insure repayment of princi-

authorizes such payment out of net profits only "if the articles so provide."¹³⁷ Even when specifically provided for, such authority is, by a concluding proviso of the subsection, "subject, however, to the rights of shareholders of different classes." It follows that, if there are common shares and shares preferred as to principal, a sufficient reserve must be maintained to insure the repayment of principal to the holders of the preferred shares. Nice problems may also arise in the determination of what property constitutes "wasting assets." Oil wells, coal or ore mines, leases and patents are expressly included. They are usually acquired for the sole purpose of being worked and consumed. On the other hand, it has been held that oil in the tanks at the formation of a corporation, and figuring as part of its capital assets, is subject to the general rule, and that the proceeds of its sale could not lawfully be distributed as dividends.¹³⁸

Dividends are formally declared by the board of directors, and the shareholder's legal right vests as of that time.¹³⁹ The declaration of dividends is a discretionary matter, and the directors may not deem it advisable to declare an immediate dividend, even though a substantial surplus is available. In general, the courts have adopted a hands-off policy and will not order the declaration of a dividend, except where bad faith or an extreme abuse of discretion is shown.¹⁴⁰

pal to preferred shareholders. The decision has been criticized with contra authority cited, Note (1926) 12 *Corn. L. Q.* 79; and approved, Note (1927) 75 *U. of Pa. L. Rev.* 350. The unsettled state of the law was recognized by the drafters of the Uniform Act, 9 *U.L.A.* 76 (Perm. ed. 1932).

137. Corresponding Section 24, VII of the Uniform Business Corporation Act, 9 *U.L.A.* 75 (Perm. ed. 1932), authorizes such payment of dividends from net profits, without the necessity of a special provision in the articles.

138. *Van Vleet v. Evangeline Oil Co.*, 129 *La.* 406, 56 *So.* 343 (1911), holding that the declaration of a dividend out of money received for oil placed in tanks prior to formation of the company and constituting part of the original capital, was gross mismanagement and necessitated the appointment of a receiver. In discussing the "wasting assets" doctrine, Judge Sommerville distinguished the oil in question from oil wells and mines which are owned for the express purpose of being worked, and of necessity become exhausted in the profit-making process.

139. After a cash dividend is declared, the shareholder becomes a creditor of the corporation for the amount of his dividend. However, prescription does not begin to run until there has been a demand and refusal. *Armant v. New Orleans & Carrollton R.R.*, 41 *La. Ann.* 1020, 7 *So.* 35 (1889). See Comment, *When Do Dividends Vest?* (1938) 27 *Geo. L. J.* 74.

Informal divisions of profits have been recognized where made in good faith and no creditors' rights were impaired. See Note (1939) 18 *Chi.-Kent Rev.* 93.

140. *Crichton v. Webb Press Co.*, 113 *La.* 167, 36 *So.* 926 (1904), the court ordered the declaration of a dividend where the directors of a corporation with an enormous surplus refused to declare dividends in an obvious effort to starve out minority shareholders. Accord: *Dodge v. Ford Motor Co.*, 204

Section 27¹⁴¹ sets forth the liability of directors and shareholders for dividends unlawfully paid or corporate assets otherwise unlawfully returned. Under subsection I, only those directors who knowingly or negligently voted in favor of such unlawful payments are made liable, and an express allegation of such knowledge or lack of care is essential to a good cause of action.¹⁴² The liability of the directors is joint and several and exists in favor of creditors of the corporation, rather than in favor of the corporation itself as in the Uniform Act.¹⁴³ This provision for direct liability to creditors has the advantage of enabling a creditor to obtain relief without resorting to the circuitous procedure of first securing a judgment against the corporation and having it returned unsatisfied. Also, the creditors are the ones primarily affected by such unlawful payments and they will likely act more promptly than those in charge of the corporation (who may be in sympathy with, if not implicated in, the payment). Probably the creditor's cause of action is for the full amount of the unlawful payment, with any excess over his claim inuring to the benefit of the corporation; for the liability is declared to be "in an amount equal to the dividends so paid." It is also possible to so interpret this provision as to make the amount of the suing creditor's claim the outside measure of liability. Much can be said in favor of those statutes which impose liability to the corporation and/or

Mich. 459, 170 N.W. 668 (1919). Cf. *Marks v. American Brewing Co.*, 126 La. 666, 52 So. 983 (1910), where the court properly refused to order a dividend declared.

141. La. Act 250 of 1928, § 27 [Dart's Stats. (1939) § 1107]. The provision refers to dividends paid in violation of "Section 24," but should read "Section 26." This is evidently a clerical error brought about by the fact that the provision is substantially taken from Section 25 of the Uniform Business Corporation Act which properly refers to Section 24 of that Act.

142. *Nola Lumber Co. v. Alexander*, 182 La. 432, 162 So. 35 (1935). In holding that the petition stated no cause of action against the directors voting in favor of an unlawful return of corporate assets to the shareholders, Rogers, J., declared (182 La. 432, 437, 162 So. 35, 36), "Section 27 of Act No. 250 of 1928, on which plaintiff founds his cause of action, applies only to those directors 'who knowingly, or without exercising that diligence, care and skill which ordinarily prudent men in like positions would exercise under similar conditions, voted in favor of' an unlawful distribution, payment, or return of assets to shareholders. We think such an allegation is essential. Under section 17 of Act No. 267 of 1914, liability attached to the director, who merely assented to the act complained of, whether his assent was given knowingly or innocently. But, when the subsequent corporation statute was drawn, the lawmakers were careful to impose liability only on those directors who knowingly or carelessly voted for the things set out in the statutory provision."

143. Uniform Business Corporation Act, § 25, I, 9 U.L.A. 77 (Perm. ed. 1932).

creditors,¹⁴⁴ thus making doubly certain the fact that the erring directors will be held fully responsible.

Where the shareholder had actual knowledge of the impropriety of the dividend, he is liable to the corporation or its creditors on the ground of fraud.¹⁴⁵ Where the shareholder innocently received the dividend or other unlawful distribution of corporate capital, his position has been uncertain.¹⁴⁶ Subdivision II of Section 27 clearly covers this situation. It provides for general shareholder liability, but only: (1) where there are no guilty or negligent directors; or (2) where directors are liable, to the extent that the creditor is unable to obtain satisfaction after recovering a judgment against the directors. The shareholder's liability expressly runs "to the corporation," rather than to creditors of the corporation, as does the director's liability. Yet, there are certain situations where, for very practical reasons, this proviso has been held inapplicable. In the case of *Fudickar v. Inabnet*¹⁴⁷ a corporation had been completely liquidated and its assets distributed among the shareholders although its debts had not been paid. The Louisiana Supreme Court allowed corporate creditors to proceed directly against the shareholders to enforce their liability arising out of the unlawful distribution. Then too, it has been suggested that the cause of action against shareholders receiving unlawful dividends or other disbursements may be availed of indirectly by an unsatisfied judgment creditor, who may levy upon it as a corporate asset.¹⁴⁸

Subsection III completes the picture, providing that "where the directors are held liable for the sole reason of acting negli-

144. Modern corporation statutes vary considerably, both as to the extent of liability and in whose favor the liability runs. 12 Fletcher, Corporations, 143, § 5432. At common law, directors were liable for a willful or negligent declaration of an unlawful dividend "not only to the corporation, but also, in equity, to creditors." *Id.* at 140, § 5431.

145. La. Act 250 of 1928, § 19, III [Dart's Stats. (1939) § 1099, III] reserves all existing causes of actions predicated upon fraud.

146. 12 Fletcher, Corporations, 129-131, § 5423.

147. 176 La. 777, 781, 146 So. 745, 746 (1933). Rogers, J., considered it "of no importance here" that under Section 27 of the Louisiana Business Corporation Act the stockholder's liability runs in favor of the corporation, since the corporation had been liquidated and ceased to exist; and declared that if, under the circumstances, the shareholders should not be held liable, "the plaintiff occupies the anomalous position of the possessor of a right without a remedy to enforce it." *Accord: Derbes v. Till*, 13 La. App. 495, 128 So. 196 (1930), where in allowing a direct action by creditors, Janvier, J., emphasized the facts that the liquidation had been terminated and that there was no one to bring suit for the corporation, and concluded (13 La. App. 495, 497, 128 So. 196, 198) "It therefore seems that the matter should be allowed to go to trial 'as a last resort, and the only means of preventing a denial of justice.'"

148. 9 U.L.A. 77 (Perm. ed. 1932), Commissioners' Notes to corresponding Section 25, II, of the Uniform Business Corporation Act.

gently," they shall have a right of action over against each of the shareholders in proportion to the amount such shareholder received.

SHAREHOLDERS' PREEMPTIVE RIGHTS

The shareholder's preemptive right to subscribe for a proportionate share of any further allotment of stock is a valuable protection and enables him to maintain the existing ratio of his proprietary interest and voting power in the corporation.¹⁴⁹ Where, however, a new issue of stock is allotted for a purpose other than, or in addition to, that of obtaining additional cash for working capital, the shareholder's assertion of a preemptive right may present serious difficulties. For example, the corporation may need a tract of land which the owner proposes to trade for a certain number of shares. Naturally, existing shareholders cannot be given the privilege of subscribing for a portion of this new allotment of stock. Section 28¹⁵⁰ of the Louisiana Business Corporation Act expressly permits the articles to include any desired provisions restricting or enlarging the preemptive right. But in the absence of some contrary provision in the articles, subsection II stipulates that the holders of voting shares shall have a preemptive right to subscribe for a proportionate number of any further allotment for cash of shares having voting rights. Following the path indicated by judicial decision, the subsection declares that a shareholder shall have no preemptive right to subscribe for shares allotted for consideration other than cash, shares allotted to satisfy conversion or option rights, or shares once allotted and then subsequently held by the corporation as treasury shares. Also, shares may be issued to corporate employees free from preemptive rights upon the written consent or vote of the holders of a majority of the shares entitled to exercise such rights. In cases where the preemptive right exists, the shareholder is given "a reasonable time to be fixed by the board of directors," to subscribe for his proportion of the new stock. If he is unable to raise sufficient funds, or for some other reason does not choose to take up the shares, the right may be assigned or sold.¹⁵¹ Where a share-

149. *Stokes v. Continental Trust Co.*, 186 N.Y. 285, 78 N.E. 1090 (1906). For a complete discussion of the shareholder's preemptive right, see 11 *Fletcher, Corporations*, 218-238, §§ 5135-5141. The right is now generally recognized as to *voting* shares, either by judicial decision or by statute. *Id.* at 218, § 5135.

150. La. Act 250 of 1928, § 28 [*Dart's Stats.* (1939) § 1108].

151. Although Section 28 of the Louisiana Business Corporation Act does not expressly provide for assignability, the implication of this right is well supported by the authorities. 11 *Fletcher, Corporations*, 233.

holder is denied his right to subscribe for additional shares, he may bring an action for damages, for specific performance, or to enjoin the wrongful derangement of his proportionate voting powers.

BY-LAWS

Under Section 29, subsection II,¹⁵² the corporation's inherent power¹⁵³ to adopt by-laws resides in the shareholders. The board of directors may be given a general power to make by-laws through an express provision in the articles, but such director-made by-laws are subject to change or repeal by the shareholders. A general provision in the articles empowering the directors to make or alter by-laws does not include a power to make or alter by-laws fixing their own qualifications, classification, term of office, or compensation. Such a power may, however, be specifically vested in the directors by the articles or shareholder-made by-laws. The Uniform Act forbids such action by the board of directors.¹⁵⁴ Subsection II provides a nonexclusive enumeration of matters which may be covered by the by-laws.

In line with a similar declaration relating to the articles,¹⁵⁵ subsection III states that third persons dealing with the corporation shall not be charged with constructive notice of the by-laws. The officers, directors, and shareholders are left subject to the general rule that they are conclusively presumed to know the corporation's by-laws or amendments thereto, and they remain actually ignorant thereof at their peril.¹⁵⁶ For example, where the corporate by-laws provide that "the tenure of all officers of this corporation shall be during the pleasure of the board of directors," the Louisiana court held that an officer holding over after a twelve months' employment contract was "presumed to have known" the precarious tenure by which he held his position, and could not complain when he was suddenly discharged.¹⁵⁷ The provision is susceptible to the construction that, where a shareholder

152. La. Act 250 of 1928, § 29, I [Dart's Stats. (1939) § 1109, I].

153. "The power to adopt by-laws is inherent in every corporation. . . ." 8 Fletcher, Corporations, 641, citing *State v. Bank of Louisiana*, 5 Mart. (N.S.) 327 (1827). But it is of such great importance that ". . . as a general rule the power is expressly conferred by the laws from which corporate existence is derived." 8 Fletcher, *supra* at 643.

154. Uniform Business Corporation Act, § 26, III, 9 U.L.A. 78 (Perm. ed. 1932). This sound prohibition might well have been adopted in the Louisiana act.

155. See Section 11, discussed *supra* p. 607.

156. For a full citation of authorities see 8 Fletcher, Corporations, 746-750, notes 48-50, 60-63.

157. *Hunter v. Sun Mutual Ins. Co.*, 26 La. Ann. 13 (1874).

deals with the corporation in a transaction not growing out of or dependent upon his shareholder relationship, he may be treated as a stranger and not charged with constructive notice of its by-laws.¹⁵⁸

SHAREHOLDERS' MEETINGS

Section 30¹⁵⁹ requires that at least one shareholders' meeting shall be held each year. The time, place, notice, and manner of calling and conducting the shareholders' meetings should be set out in the by-laws.¹⁶⁰ It is the plain ministerial duty of the directors, president, or such other officer as is designated in the by-laws, to call the annual meetings at the designated time. A writ of mandamus will issue at the instance of a stockholder to compel the calling of a shareholders' meeting, and it is no defense that the officer charged with the duty was fearful as to the action the shareholders might take.¹⁶¹ Whenever more than eighteen months pass without the annual shareholders' meeting having been held, any shareholder may call such meeting.¹⁶² Also, special meetings must be called by the Secretary, upon the written request of any director, or of any shareholder or shareholders holding one-fifth of the voting power of all shareholders.¹⁶³ With the exception of adjourned meetings,¹⁶⁴ and unless otherwise provided in the articles or by-laws, the person calling a shareholders' meeting shall cause a written notice of the time, place, and purpose of

158. *Pearsall v. Western Union Tel. Co.*, 124 N.Y. 256, 26 N.E. 534 (1891). A shareholder dealing with the telegraph company as a customer in sending messages was held not to be chargeable with constructive notice of a resolution by the board of directors that the company would not be liable for mistakes in unrepeatable messages.

159. La. Act 250 of 1928, § 30, I [Dart's Stats. (1939) § 1110, I].

160. *Id.* at § 29, II(a) [Dart's Stats. (1939) § 1109, II(a)]. Where the date, but not the hour, of the meeting was set out in the by-laws, the directors could fix the time of meeting at 9 o'clock, A. M., that being a reasonable hour. *State v. Simms*, 152 So. 395 (La. App. 1934).

161. *State v. J. D. Kerr Gravel Co.*, 158 La. 324, 104 So. 60 (1925), *St. Paul, J.*, declared (158 La. 324, 326, 104 So. 60, 61): "The sum and substance of the defense is that the president fears that said stockholders will elect a board of directors and officers who may be unfavorable to himself and his interests, and that he has never been requested in writing to call said meeting."

"Such a position is, of course, untenable. It is the plain ministerial duty of the president to call said meeting, whether requested to do so or not; and, if the stockholders do anything they have no right to do, it will then be his privilege to complain." For a full collection of cases in point see 5 *Fletcher, Corporations*, 14, 15.

162. La. Act 250 of 1928, § 30, II [Dart's Stats. (1939) § 1110, II].

163. *Ibid.* Applied in *Davidson v. American Paper Mfg. Co.*, 188 La. 69, 175 So. 753 (1937); *Best v. Southern Hide Co.*, 170 La. 997, 129 So. 614 (1930).

164. La. Act. 250 of 1928, § 30, III [Dart's Stats. (1939) § 1110, III]. The provision that no notice of an adjourned meeting need be given is in accord with the general rule. 5 *Fletcher, Corporations*, 77.

such meeting to be given to all voting shareholders at least ten days prior to the date fixed. The right to such notice may be waived in writing by any shareholder.¹⁶⁵

The safest procedure in calling and holding a shareholders' meeting is to comply strictly with all the requirements of Section 30. Failure to give proper notice may be a ground for setting aside an election of directors.¹⁶⁶ Such a result, however, does not always follow procedural irregularities. Where the substantial rights of stockholders are not affected,¹⁶⁷ or where all shareholders are present and concur in the action taken, the validity of the proceedings is not affected by a failure to comply with directory provisions.¹⁶⁸ The requirement of subsection V, that a stockholders' list shall be produced upon the request of any shareholder, will probably be treated as directory. A New Jersey court has held that noncompliance with such a requirement, or the fact that the list furnished is false, will not, of itself, render the shareholders' meeting and the proceedings therein invalid.¹⁶⁹

The presence of a quorum is essential to the transaction of corporate business,¹⁷⁰ and there can be no valid shareholder's meeting unless this requirement is met.¹⁷¹ Section 31¹⁷² adopts the general rule, previously recognized in Louisiana,¹⁷³ that, in the absence of an express stipulation to the contrary, "the presence, in person or by proxy, of the holders of a majority of the voting power shall constitute a quorum." Final control is in the shareholders, who may adopt a greater or lesser requirement by an appropriate provision in the articles or by-laws. Once the meeting is duly organized, there are to be no technical barriers to the expeditious and complete transaction of corporate business. Clause

165. La. Act 250 of 1928, § 30, IV [Dart's Stats. (1939) § 1110, IV].

166. *Best v. Southern Hide Co.*, 170 La. 997, 129 So. 614 (1930). The irregularity complained of was that the notice was not addressed to the proper party. The court held that the complaining shareholder's remedy "is not to ask for a receiver, but to demand a new stockholders' meeting [plaintiff controlled 24% of the corporate stock], or she may bring suit to set aside the election of J. B. Best as director." (170 La. 997, 1004, 129 So. 614, 617.)

167. *Bartlett v. Fourton*, 115 La. 26, 38 So. 882 (1905).

168. 5 *Fletcher, Corporations*, 95, § 2024.

169. *Downing v. Potts*, 23 N.J. Law 66 (1851).

170. La. Act 250 of 1928, § 31, I [Dart's Stats. (1939) § 1111, I]. Clause II(c) provides for adjournment when a quorum is not present.

171. *Davidson v. American Paper Mfg. Co.*, 188 La. 69, 175 So. 753 (1937); *Hill v. Town*, 172 Mich. 508, 138 N.W. 334 (1912).

172. La. Act 250 of 1928, § 31, II(a) [Dart's Stats. (1939) § 1111, II(a)].

173. *Peirce v. New Orleans Building Co.*, 9 La. 397 (1836), holding that the shareholders could not take valid, corporate action when less than a majority were present, and that the subsequent individual assent of a majority of the shareholders did not validate the minority action.

(b) states that if a quorum is present at the organization of the meeting, the subsequent retirement of enough shareholders to leave less than a quorum does not prevent those remaining from transacting business. This forestalls the possibility that a group of obstructionist shareholders might prevent valid action by withdrawing from the meeting.¹⁷⁴ Similarly, clause (d) expressly declares that a majority of the votes actually cast, and not necessarily a majority of the votes represented, shall decide any matter brought before the meeting. Express care is taken that meetings called for the important purpose of electing directors shall not be frustrated by indefinite and repeated adjournments for the lack of a quorum. Such meetings may be adjourned only from day to day.¹⁷⁵ Also, those attending the second adjourned meeting, although less than a quorum, shall proceed to elect directors.¹⁷⁶

CORPORATE ACTION BY UNANIMOUS CONSENT

Section 64¹⁷⁷ provides that corporate action requiring shareholder authorization may be had by the unanimous written consent of the voting shareholders, without the necessity of a shareholders' meeting. Shareholder action by unanimous consent is not provided for in the Uniform Act, and such a procedure is beset with practical difficulties with respect to large corporations. It may, however, offer a useful device to smaller companies. The formal requirements of this section must be strictly complied with. In *Renauld v. Marine Specialty & Mill Supply Co.*¹⁷⁸ the Louisiana Supreme Court held that a shareholders' meeting could be dispensed with only by a written agreement, signed in duplicate by all the shareholders, and accompanied by a certificate of

174. There was some conflict at common law. Compare *Commonwealth v. Vandegrift*, 232 Pa. 53, 81 Atl. 153 (1911), applying the majority view that those remaining may continue to transact business; with *Bridgers v. Staton*, 150 N.C. 216, 63 S.E. 892 (1909), holding that a quorum must be present at the time of voting. See also Commissioners' Notes to corresponding Section 30 of the Uniform Business Corporation Act, 9 U.L.A. 84 (Perm. ed. 1932).

175. La. Act 250 of 1928, § 30, III [Dart's Stats. (1939) § 1110, III].

176. *Id.* at § 31, II(c) [Dart's Stats. (1939) § 1111, II(c)]: "Without the last clause of this subdivision, an entrenched board of directors could prevent the holding of an election. . . . It has been held that, except where the statute, charter or by-laws provide otherwise, those shareholders present at a duly called annual meeting held for the election of directors have not only the right but the duty to elect directors, and the majority may not, by absenting themselves from such meeting, prevent such election." Commissioners' Notes to corresponding Section 30, II(c) of the Uniform Act, 9 U.L.A. 84, 85 (Perm. ed. 1932).

177. La. Act 250 of 1928, § 64 [Dart's Stats. (1939) § 1144].

178. 172 La. 835, 135 So. 374 (1931), holding that the unanimous oral consent of the shareholders was not binding on the corporation.

the corporation secretary to the effect that the subscribers constituted all the shareholders entitled to vote on the particular question.

VOTING RIGHTS

Section 32, I,¹⁷⁹ declares that, unless otherwise provided in the articles, "each shareholder of record shall be entitled to one vote for each share of stock standing in his name on the corporate books." It is not uncommon, however, to deprive the preferred stock of voting rights, and the articles may be so drawn as to concentrate the voting power in a relatively small class of shareholders.¹⁸⁰ Those shares excluded from general voting powers are afforded a measure of protection by the requirement in Section 42 that important amendments to the articles must be approved by every class of shareholders, whether voting or non-voting.¹⁸¹

Cumulative voting in the election of directors affords minority interests the opportunity to secure representation on the board of directors. The operation is simple: a shareholder is permitted to multiply the number of votes to which he is entitled, by the total number of directors to be elected. He may cast all such votes for one, or possibly more, candidates. For example, a minority shareholder or group holding 20% of the stock is mathematically certain to be able to elect one of five directors; while under the ordinary method of voting, the majority could elect all five. Through the director thus elected, the minority has a direct contact with the business, and is able to secure first hand information as to management and operation of the company.

The Louisiana provision¹⁸² is permissive, in that it merely authorizes a grant of cumulative voting privileges. The privilege

179. La. Act 250 of 1928, § 32, I [Dart's Stats. (1939) § 1112, I]. This provision has been very properly held inapplicable to an insurance company. *State v. Carradine*, 12 La. App. 42, 125 So. 135 (1929). See also La. Act 250 of 1928, § 2 [Dart's Stats. (1939) § 1081].

180. La. Act 250 of 1928, § 3, I(f) [Dart's Stats. (1939) § 1080, I(f)], provides that the articles shall contain a description of the various classes of shares "and the designations, voting powers, preferences, . . ." etc. of each class. The articles may provide for the issuance of a substantial class of shares without or with only limited voting powers.

181. La. Act 250 of 1928, § 42, III, IV [Dart's Stats. (1939) § 1122, III, IV]. Subsection III provides that where an amendment would make a change in the rights of a particular class of shares, a class vote of the shareholders affected is necessary for its adoption. Subsection IV provides that where an amendment would make a change in the corporate name or a substantial change in the corporate purpose or purposes, a two-thirds vote of every class of shares, voting by classes, is necessary for its adoption.

182. La. Act 250 of 1928, § 32, II [Dart's Stats. (1939) § 1112, II], reads, "The articles *may provide*. . ."

must be expressly provided for in the articles, and an attempt to confer the right through a by-law will be ineffective.¹⁸³ The Uniform Act contains a provision of the mandatory type, granting an absolute right to vote cumulatively to the shareholders of all corporations.¹⁸⁴ The cumulative voting right provides a valuable safeguard for minority interests, and there is much to be said for the mandatory grant. It does not depend upon the will of the incorporators and is not subject to being withdrawn by the majority through an amendment of the articles.¹⁸⁵

The early common law rule that a shareholder must vote in person¹⁸⁶ has been changed by modern corporation statutes. Section 32, subsection III of the Louisiana Act authorizes voting by proxy.¹⁸⁷ No particular form or words are necessary to constitute a proxy; but it must be in writing, signed by the shareholder, and filed with the secretary. The Act expressly stipulates that the proxy shall be revocable at will, notwithstanding any agreement or provision to the contrary. Thus, even a proxy "based upon a consideration" or "coupled with an interest" is revocable.¹⁸⁸ The

183. *In re Brophy*, 13 N.J. Misc. 462, 179 Atl. 128 (1935), interpreting a similar permissive type statute.

184. Uniform Business Corporation Act, § 28, III, 9 U.L.A. 79 (Perm. ed. 1932). Seventeen states have mandatory enactments (by statute or constitutional provision), while fifteen fall in the permissive classification. *Bowes and De Dow, Cumulative Voting at Elections of Directors of Corporations* (1937) 21 Minn. L. Rev. 351, 352, notes 6 and 9.

185. "While it is possible to conceive of situations in which the grant of the privilege of voting cumulatively might turn out to be valueless or a needless refinement, it is difficult to imagine any situation in which that privilege would be a burden or handicap to persons other than those comprising a majority group which desires to exclude the minority from any participation in the management of corporate affairs in derogation of the very purpose underlying such enactments. This being the case, if the privilege is to be granted at all, the grant should not be at the will of incorporators who may compose the majority group, nor should a majority be afforded the opportunity to withdraw any such grant at its pleasure by amending the corporate charter or by-laws." *Bowes and De Bow*, supra note 184, at 370.

The blanket amending power granted by Section 42 of the Louisiana Act would enable the holders of two-thirds of the voting shares to repeal a provision authorizing cumulative voting.

186. *Taylor v. Griswold*, 14 N.J. Law 222, 27 Am. Dec. 33 (1834). The decisions were conflicting as to whether authority to vote by proxy could be conferred by a by-law, in the absence of express statutory sanction. 9 U.L.A. 81 (Perm. ed. 1932).

187. For a discussion of some of the problems and abuses arising out of proxy voting, see *Bernstein and Fisher, The Regulation of Solicitation of Proxies* (1940) 7 U. of Chi. L. Rev. 226.

188. It is the general rule that a proxy is irrevocable where "based upon a consideration" or "coupled with an interest." 5 *Fletcher, Corporations*, 188, n. 99. The Uniform Business Corporation Act, § 28, IV, recognizes the revocability of a proxy "coupled with an interest." 9 U.L.A. 79 (Perm. ed. 1932).

provision that the validity of a proxy stating no definite period of duration shall automatically cease eleven months after its execution, puts a desirable check upon the continued effectiveness of stale proxies. There is no restriction upon the stated duration of a proxy, except that the proxy may always be revoked by a written notice to the secretary or the filing of a later proxy.

Subsection V of Section 32 stipulates that a person in whose name shares are registered in a fiduciary capacity may vote the same.¹⁸⁹ Nevertheless, the Louisiana Supreme Court, following a well-settled rule of general jurisprudence, has held that an administrator or executor is entitled to vote shares owned by a succession, without the necessity of a formal transfer of the stock on the corporate books.¹⁹⁰

Bondholders are without voting rights, and such power may be conferred upon them only by express consent of the state. Subsection VIII empowers the corporation to provide in its articles for granting of voting rights to bondholders. It is not uncommon to authorize a transfer of full voting rights, or the power to elect a majority of the board of directors, to bondholders in case of default in interest payments to them for a specified number of times. Such provisions enable the bondholders to assume management of the corporation until the defaults are made good, whereupon their voting rights terminate, and the voting control reverts to the shareholders.¹⁹¹ By such an arrangement expensive and unsatisfactory receivership proceedings may often be averted.

The voting trust is generally regarded as a device to be used, and sometimes abused, for vote control. There has been considerable conflict, at least in the verbiage of the decided cases, concerning the validity of voting trust agreements. Some courts have held them void. In doing so they usually announce the policy argument that participating shareholders breach their duty to other owners of stock when they strip themselves of the power to

189. Subsections IV and VI, dealing with the voting of pledged shares and shares owned by one corporation in another, are self-explanatory. Subsection VII declares that treasury and unissued shares shall not be voted or counted in calculating voting power.

190. *Davidson v. American Paper Mfg. Co.*, 188 La. 69, 175 So. 753 (1937).

191. For a fine discussion of the problem, with suggested provisions and procedure, see Tracy, *The Problem of Granting Voting Rights to Bondholders* (1935) 2 U. of Chi. L. Rev. 208, 212-216.

Similar authority for granting voting rights to security holders has also been conferred by statute in Delaware, Michigan, Nevada, Ohio, and Virginia (Statutes collected by Tracy, *supra* at 213). The Uniform Business Corporation Act does not contain such a provision.

exercise the voting prerogative.¹⁹² The modern and better view is that such agreements are valid where the purpose is proper.¹⁹³ Subjected to necessary limitations as to purpose, the voting trust may be very useful, and provides an effective means for the scattered shareholders in a large corporation to secure a voice in its operation. There is nothing illegal in a combination by shareholders for the purpose of securing management of the corporation by responsible persons as directors.¹⁹⁴ Yet an agreement contemplating the election of directors obligated to select one of the contracting parties as president was properly held void and unenforceable by the Louisiana Supreme Court in *Williams v. Fredericks*.¹⁹⁵ Chief Justice O'Niell stressed the generally accepted idea that the authority and fiduciary duty of directors to exercise a free and disinterested discretion in the selection of corporate officers should not be bartered away.

Section 33¹⁹⁶ of the Louisiana Act, in common with practically all modern corporation statutes,¹⁹⁷ expressly authorizes the voting trust. Trusts formed under this provision are irrevocable for the period stated in the agreement,¹⁹⁸ but may not exceed ten years in duration. A voting trust for a longer period would probably be held totally invalid.¹⁹⁹ The requirements that the agreement among the shareholders (which is essential to a voting trust) shall be in writing and filed in the registered office of the corporation, must be strictly complied with if a valid trust is to be

192. For collection of cases in point, see 5 Fletcher, Corporations, § 2078, notes 53-57, 275-276. The various arguments against the validity of the voting trust are raised and answered in an article by Burke, Voting Trusts Currently Observed (1940) 22 Minn. L. Rev. 347, 354 et seq.

193. "The tide of opinion is now away from condemnation towards a discerning approval." 5 Fletcher, Corporations, 276, citing Mackin v. Nicollet Hotel, 25 F.(2d) 783 (C.C.A. 8th, 1928). Accord: Alderman v. Alderman, 178 S.C. 9, 181 S.E. 897 (1935), noted favorably (1936) 34 Mich. L. Rev. 727.

194. See *Williams v. Fredericks*, 187 La. 987, 988, 175 So. 642, 646 (1937).

195. 187 La. 987, 989, 175 So. 642, 644. Accord: *Cone v. Russell*, 48 N.J. Eq. 208, 21 Atl. 847 (1891), agreement for proxy, providing that the directors to be elected should employ the one giving the proxy at a fixed salary, held invalid; *McQuade v. Stoneham*, 263 N.Y. 323, 189 N.E. 234 (1934), noted (1934) 11 N.Y.U. L.Q. Rev. 640, mutual agreement of majority stockholders to continue each other as directors and officers, held invalid.

196. La. Act 250 of 1928, § 33 [Dart's Stats. (1939) § 1113].

197. See Burke, *supra* note 192, at 348, 360, for a history and collection of such statutory provisions.

198. In re *Morse*, 247 N.Y. 290, 160 N.E. 374 (1928).

199. A voting trust for a period of 11 years, when the Delaware statute imposed a time limitation of 10 years, was held to be wholly invalid, not merely void as to the excess period. *Perry v. Missouri-Kansas Pipe Line Co.*, 191 Atl. 823 (Del. Ch. 1937).

created.²⁰⁰ The trustee must accept the trust. This may be done by his acting under the trust,²⁰¹ but, the presence of his signature on the agreement is decidedly preferable.

In a voting trust, created under Section 33, there is no separation of the voting power from the stock. The shareholders, pursuant to the agreement, transfer their certificates to the trustee or trustees, to be cancelled and reissued in the name of the trustee with proper reference to the agreement on the new certificates.²⁰² The trustee then issues voting trust certificates to the shareholders in lieu of the stock certificates thus transferred. These certificates are transferable in the same manner and with the same effect as share certificates.²⁰³ The net result is that the voting power is in the trustee in whose name the shares now stand,²⁰⁴ while the beneficial interest is in the trust certificate holders who receive the dividends, less the expenses of administering the trust.

The voting trust is continuously subject to potential enlargement, until all shareholders become parties to it. Subsection III provides that other shareholders shall at any time have the right to come into the trust arrangement upon the same terms and with the same benefits as the shareholders originally participating. This prevents the participants from arbitrarily excluding certain minority shareholders. At the same time it makes it possible for majority shareholders to gain control of a voting trust originally organized by a minority group.

DIRECTORS, OFFICERS, AND AGENTS

Section 34 vests the general management of the business and affairs of the corporation exclusively in a board of directors elected by the shareholders.²⁰⁵ Subsection I fixes the minimum number of directors at three, but sets no outside limit. The directors need not be shareholders and need not be residents of Louisiana. Special restrictions may be imposed by the articles or by-laws.²⁰⁶ The term of office is one year, unless otherwise provided,

200. In *Williams v. Fredericks*, 187 La. 987, 1001, 175 So. 642, 647, it was held that an agreement could not be sustained as a voting trust under Section 33, since it was not "in writing" and "filed at the registered office of the corporation." Valuable precautions in the drawing of a voting trust agreement are suggested by *Burke*, supra note 192, at 374.

201. In *re Bartleson Co.*, 275 Fed. 390 (1920).

202. La. Act 250 of 1928, § 33, I, III, IV [Dart's Stats. (1939) § 1113, I, III, IV].

203. *Id.* at § 33, V [Dart's Stats. (1939) § 1113, VI].

204. *Id.* at § 33, VI, VII [Dart's Stats. (1939) § 1113, VI, VII].

205. *Id.* at § 34, I, II [Dart's Stats. (1939) § 1114, I, II]. Under subsection III(a) vacancies in the board are filled by the remaining directors.

206. The general rules of subsection I are prefaced by "unless otherwise provided" clauses. Sections 29, II(d), and 34, III, state that the by-laws may

but cannot exceed five years. Subsection III lays down certain rules which apply "except as otherwise prescribed in the articles or by-laws." Clause (c) permits meetings of the board to be held at any place agreeable to a majority of the directors, whether in or outside the state. Voting by proxy may be authorized by an express provision in the articles, but otherwise is not permitted.²⁰⁷ Clause (d) applies the general common law rule that a majority of the directors is necessary for a quorum. Where the quorum requirement has been met, valid action may be taken by a majority vote of those directors present, and this is so even though some have withdrawn, leaving less than a quorum. Clause (e) provides that the board may delegate powers to committees made up of two or more directors.

In the exercise of their powers of management, the directors are entirely free from direct shareholder control. Even a unanimous resolution of the shareholders does not bind the corporation in such matters,²⁰⁸ and may be ignored by the board. A means of immediate control of recalcitrant directors is furnished by the provision in subsection III, clause (b), for the removal of directors, with or without cause, by a two-thirds vote of the shareholders. A proper limitation on this power is the stipulation that a director elected by the exercise of the cumulative voting privilege may be removed only for cause. The board of directors is also authorized to remove a member for certain specified causes.²⁰⁹

Section 35²¹⁰ vests the power of appointment and removal of the officers and necessary agents of the corporation in the board of directors. Only the president need be a director. The duties and authority of such officers and agents may be prescribed in the articles or by-laws, but in the absence of such provisions are to be determined by the directors. Where there is no express authoriza-

provide the number, classification, tenure of office, qualifications, and compensation of directors. For example, the by-laws might prescribe Louisiana residence as a necessary qualification. Opinions of the Attorney General, 1934-36, p. 160.

207. La. Act 250 of 1928, § 35, VI [Dart's Stats. (1939) § 1115, VI].

208. *Gashwiler v. Willis*, 33 Cal. 11, 91 Am. Dec. 607 (1867). For a complete discussion of the power of shareholders to bind a corporation, see Note (1917) 15 Mich. L. Rev. 264; 5 Fletcher, Corporations, 348.

209. La. Act 250 of 1928, § 34, III(a) [Dart's Stats. (1939) § 1114, III(a)]: ". . . the board of directors may declare vacant the office of a director: (1) if he be interdicted or be adjudicated a bankrupt; or (2) if he be absent from the State continuously for a period of six months without leave granted by the board, or if he become incapacitated by illness or other infirmity to perform his duties for a like period; or (3) if he cease at any time to have the qualifications required by the articles or by-laws."

210. *Id.* at § 35, I-III [Dart's Stats. (1939) § 1115, I-III].

tion, either in the by-laws or by resolution of the directors, the courts sometimes recognize authority based upon a sanction of the past practice, custom, and dealings of the corporation. In a Louisiana case, where it was shown to have been the usual practice for the general manager to conduct corporate affairs with little advice or supervision from the board of directors, the court overruled a defense that a note given by him to the plaintiff for insurance premiums advanced to the corporation was not authorized by the directors.²¹¹ An estoppel element is invariably present and stressed in such decisions.²¹² The estoppel arises from the fact that the company has generally enjoyed the benefit of the action of such officers and agents. Subsection VII empowers the president, vice-president, or manager to take all reasonable and necessary steps to represent the corporation in legal matters. Unless expressly limited by the articles, by-laws, or resolution of the board of directors, such officers may authorize the institution of suits or appeals from adverse judgments,²¹³ and direct the issuance of conservatory writs. Such powers cannot be exercised by subordinate officers, at least when those named are not absent from the state.²¹⁴

Section 36²¹⁵ serves a very necessary purpose in view of the unsettled state of the case law regarding the relationship of directors and officers to the corporation, and the standard of care to which they are held. There has been considerable conflict in judicial declarations as to the status of a director or officer. Many

211. *Harris v. H. C. Talton Wholesale Grocery Co.*, 123 So. 480 (La. App. 1929). The manager was, incidentally, the second largest shareholder in the corporation.

212. *Id.* at 482. Quoting from *Gueydan v. T. P. Ranch Co.*, 156 La. 397, 100 So. 541 (1924), where the court stated, "A corporation may not, any more than an individual, reap the benefits flowing from the acts of its officers and repudiate the obligations arising from the same acts. . . . A course of conduct pursued by a corporation for many years, in permitting an officer to do an authorized [not *ultra vires*] act, is an acquiescence in such act and creates an estoppel."

213. *Pierson v. Victory Industrial Life Ins. Co.*, 18 La. App. 327, 134 So. 425 (1931). The court relied on Section 35, VII, in holding that the president of a corporation could appeal from an adverse judgment and sign the appeal bond, without specific authorization by the board of directors.

214. *Donohoe Oil & Gas Co. v. Mack-Jourden Co.*, 144 So. 169 (La. App. 1932), reversing former opinion 142 So. 713 (La. App. 1931). The court dissolved a writ of sequestration issued on the affidavit of a subordinate employee as "acting manager." It was intimated that the writ might have been sustained upon a showing that the officers authorized by Section 35, VII, were absent at the time.

215. La. Act 250 of 1928, § 36 [Dart's Stats. (1939) § 1116].

decisions refer to him as an "agent."²¹⁶ Probably a majority of opinions describe him as a "trustee."²¹⁷ Both terms, if strictly applied, are misleading and inaccurate. In line with an increasing tendency of both courts and writers to emphasize the fiduciary character of the director's status, instead of forcing it into one of the conventional classifications,²¹⁸ Section 36 declares that "officers and directors shall be deemed to stand in a fiduciary relation to the corporation." Thus, without the abstruse niceties and exactitudes of a stereotyped classification, the courts can hold the corporate officer or director to a practical standard of good faith, loyalty, and honesty. The clear phraseology of the Louisiana provision should facilitate accurate and consistent judicial expression, but will have little effect upon the actual decisions. In certain frequently recurring situations the lines have become pretty well drawn, and it does not appear to have made a great deal of difference whether the corporate director was characterized as a "trustee," "agent," or "fiduciary."

A Louisiana court has recently approved the generally accepted proposition that an officer or director may make a valid contract with the corporation if the latter is represented by a disinterested majority of the board of directors or by other independent, competent agents.²¹⁹ However, such contracts are subject

216. *Ellett v. Newland*, 171 La. 1019, 132 So. 761 (1931), where the directors and officers of a banking corporation were characterized as "agents." Accord: *Ten Eyck v. Pontiac R.R.*, 74 Mich. 226, 41 N.W. 905 (1889); *Briggs v. Spaulding*, 141 U.S. 132, 11 S.Ct. 924, 35 L.Ed. 662 (1891).

217. *Bent v. Priest*, 86 Mo. 475 (1885). For a full collection of cases in point, see Uhlman, *The Legal Status of Corporate Directors* (1939) 18 B. U. L. Rev. 12, 13, n. 12.

218. The article by Uhlman, *supra* note 217, is a very complete and able discussion of the conflicting views as to the legal status of the corporate director. The writer reaffirms the apt suggestion by Johnson, *Corporate Directors as Trustees in Illinois* (1929) 23 Ill. L. Rev. 653, 671, that "A director classified as a trustee is a round peg in a square hole; and put with the agent he is sometimes a square peg in a round hole. . . ." See also Note (1939) 39 Col. L. Rev. 219, where the inapplicability of the trustee concept is pointed out.

For a collection of cases where the court simply designated the directors as fiduciaries, see Uhlman, *supra* at 16, n. 28.

219. *General Motors Acceptance Corp. v. Hahn*, 190 So. 869 (La. App. 1939), noted (1940) 2 LOUISIANA LAW REVIEW 374. See also 3 Fletcher, *Corporations*, 287. Cf. *In Allardyce v. Abrahams*, 190 La. 686, 182 So. 717 (1938), discussed by the writer in *Work of the Louisiana Supreme Court* (1939) 1 LOUISIANA LAW REVIEW 314, 404, the Louisiana Supreme Court indicated a tendency to bear unduly hard on the conscientious officer or director. There, a general manager had personally paid off a corporate note to stave off an anxious creditor, and had received the note. Although the court allowed the purchasing officer to recover on the note, it stressed the fact that there was

to close scrutiny by the courts; and, notwithstanding their approval by a disinterested majority of the board of directors, will be set aside upon proof of the slightest unfairness or imposition practiced on the corporation.²²⁰

The right of a director to take personal advantage of corporate opportunities has been much litigated and discussed.²²¹ Here the director or officer has not been judged by the same strict standards as the trustee under an express trust. Yet he is not entirely free to avail himself of such opportunities. In *Lawrence v. Sutton-Zwolle Oil Company*²²² the Louisiana Supreme Court held that the directors of an oil company could individually secure available oil leases and were under no duty to acquire them for the benefit of the corporation. In so deciding, Justice Fournet applied the general rule that "whether in any case an officer of a corporation is duty bound to purchase property for the corporation, or to refrain from purchasing property for himself, depends upon whether the corporation has an interest, actual or in expectancy, in the property, or whether the purchase of the property by the officer may hinder or defeat the plans and purpose of the corporation in the carrying on or development of the legitimate business for which it was created."²²³ The abstract rule is best understood by a classification and analysis of actual decisions. It has been held that a mere negotiation or desire for the purchase or lease of property does not create such an expectancy in favor of the corporation as to preclude acquisition of the property by its officers.²²⁴ But, where the corporation has expended money and substantial effort in an attempt to acquire the property, an expectancy is

no offer to reimburse him for the money paid out; and declared, by way of dictum, that such a transaction might be set aside as voidable. It is suggested that there had been no breach of the officer's fiduciary relation and that the transaction should have been treated as entirely valid. *Twin-Lick Oil Co. v. Marbury*, 91 U.S. 537, 23 L.Ed. 328 (1875).

220. *Crescent City Brewing Co. v. Flanner*, 44 La. Ann. 22, 10 So. 384 (1892). The directors of a corporation in bad financial condition authorized the sale of property costing \$100,000.00, and necessary to the corporate business, to one of the directors for \$20,000.00. The sale was set aside upon its repudiation by a new board of directors.

221. *Lake, The Use for Personal Profit of Knowledge Gained While a Director* (1937) 9 Miss. L. J. 427; Comment (1939) 39 Col. L. Rev. 219.

222. 193 La. 117, 190 So. 351 (1939), discussed by the writer in *Work of the Louisiana Supreme Court* (1939) 2 LOUISIANA LAW REVIEW 31, 131.

223. 193 La. 117, 133, 190 So. 351, 356, the rule followed was quoted from 3 *Fletcher, Corporations*, § 861.

224. *Colorado & Utah Coal Co. v. Harris*, 97 Colo. 309, 49 P. (2d) 429 (1935); *Pioneer Oil & Gas Co. v. Anderson*, 168 Miss. 334, 151 So. 161 (1933); *Tierney v. United Pocahontas Coal Co.*, 85 W. Va. 545, 102 S.E. 249 (1920).

recognized.²²⁵ Where property is necessary and essential to the corporate business (as distinguished from property which is merely desirable or useful) its acquisition by corporate officers would hinder the business and development of the corporation and comes under the second clause of the general prohibition. Again, directors and officers may not engage in a competing business and must account to the corporation for profits thus diverted.²²⁶ It was held in a recent Louisiana case²²⁷ that an officer who received payment for revealing corporate assets to a judgment creditor had made a secret profit "in disregard of his fiduciary relation" and must account to the corporation.

In determining the degree of care which directors and officers must exercise, courts have run the gamut, from the rigorous requirement that such officers must exercise the care which the ordinary prudent man would use "in his own business,"²²⁸ to the view that they are to be held only in case of "gross negligence."²²⁹ Section 36 adopted the middle ground rule, enunciated in the leading case of *Briggs v. Spaulding*,²³⁰ that officers and directors must discharge their duties with that amount of care which "ordinarily prudent men would exercise under similar circumstances in like positions." A mere error in judgment will not render the officer or director liable.²³¹

The cause of action against officers and directors for losses

225. *De Bardeleben v. Bessemer Land & Improvement Co.*, 140 Ala. 621, 37 So. 511 (1904). A corporate tenant in possession under a lease has an expectancy of renewal, even though it may have no legal right to renew as against the lessor. *Lagarde v. Anniston Lime & Stone Co.*, 126 Ala. 496, 28 So. 199 (1900); *Robinson v. Jewett*, 116 N.Y. 40, 22 N.E. 224 (1889).

226. *Coleman v. Hangar*, 210 Ky. 309, 275 S.W. 784 (1925). The resultant "adversity of interest" is important in such cases; the director cannot faithfully serve two gods and is likely to favor that of self-interest.

227. *Louisiana Mortg. Corp. v. Pickens*, 167 So. 914 (La. App. 1936). Dore, J., pointed out that it was unimportant that the corporation showed no injury, since the debt enforced was an honest one, and that the officer could have been forced to disclose the corporate assets. "The important fact is that Trotti owed the duty to the corporation of which he was an officer to give it the benefit of any and all profits which he made in dealing with the affairs of the corporation." (167 So. 914, 915).

228. *Hun v. Cary*, 82 N.Y. 65, 71 (1880). Also dissenting opinion of Harlan, J., in *Briggs v. Spaulding*, 141 U.S. 132, 11 S.Ct. 924, 35 L.Ed. 662 (1891).

229. *Spring's Appeal*, 71 Pa. 11, 10 Am. Rep. 684 (1872).

230. 141 U.S. 132, 11 S.Ct. 924, 35 L.Ed. 662 (1891).

231. *Reliance Homestead Ass'n v. Nelson*, 179 La. 680, 154 So. 734 (1934). The president of plaintiff, Homestead Ass'n, was not liable for an error in judgment in making an untimely payment to a borrower. The court found that the defendant had acted with reasonable care and in good faith. Accord: *Percy v. Millaudon*, 8 Mart. (N.S.) 68, 78 (1829), Porter, J., declared: "The test of responsibility therefore should be, not the certainty of wisdom in others, but the possession of ordinary knowledge. . ."

occasioned by their nonfeasance or misfeasance belongs to the corporation, and the shareholders cannot sue as individuals to recover the resultant depreciation in the value of their shares.²³² In the background lurks the important practical consideration that to allow individual shareholders' actions would result in a multiplicity of suits. Where the corporate officers refuse to sue, the shareholder may bring a representative suit to enforce the corporate cause of action.

REGISTERED OFFICE AND RESIDENT AGENT

Section 37²³³ requires every corporation to maintain a registered office and appoint two or more resident agents for the service of process. The location and post-office address of the registered office must be stated in the articles, and a written notice thereof filed with the clerk of the district court in the parish where such office is situated. A change in the place of the registered office may be effected by a vote of the board of directors without the formality of an amendment to the articles. Notice of the change and the post-office address of the new registered office must be filed with the Secretary of State and with the clerk of court in the parish in which it is located. In *Canal Bank & Trust Co. v. Greco*²³⁴ the Louisiana Supreme Court recognized a change of domicile where the resolution had been adopted at a shareholders', rather than at a directors', meeting. Justice Overton emphasized the fact that all the directors were present and took part in the unanimous adoption of the resolution, and declared that the vote of the stockholders as such should be "deemed to be surplusage." The court's liberal attitude was voiced in the conclusion, "We think that there has been, while, perhaps, not a literal compliance with the statute yet a substantial compliance with it. . . ."

Subsection II requires the appointment of not less than two natural persons, of full age, and residents of the parish, to act as agents, upon whom legal process or other demands upon the corporation may be served.²³⁵ The formalities prescribed in connec-

232. *Smith v. Hurd*, 53 Mass. 371, 46 Am. Dec. 690 (1847).

233. La. Act 250 of 1928, § 37 [Dart's Stats. (1939) § 1117]. This section supplements Section 3, I(c) and (d); and is, in turn, supplemented by the definition of "Registered Office" in Section 1, XIV.

234. 177 La. 507, 148 So. 693 (1933). Cf. *Gashwiler v. Willis*, 33 Cal. 11, 91 Am. Dec. 607 (1867), supra note 208. For a general discussion of the necessity of a formal directors' meeting, see Ballantine, *Private Corporations* (1927) 326, § 100.

235. Where by death, resignation, or removal from the parish, the number of resident agents is reduced to less than two, a new agent or agents must be appointed within 30 days.

tion with the appointment of resident agents and their successors are the same as those for the establishment and change of the registered office. Where the agents for service of process have been duly appointed, service upon any other officer of the corporation will be held invalid.²³⁶ Also, domiciliary service at the home of one of the authorized agents, temporarily absent at the time, is ineffective.²³⁷

Where the corporation has failed to designate agents, or a vacancy has occurred, subsection III authorizes the service of process "upon any officer, director or resident agent named in the articles or the last report previously filed with the Secretary of State, or on any employee over the age of sixteen years found in the corporation's registered office or in any place where the business of the corporation is regularly conducted." Relying upon the above provision, a Louisiana court has held that service upon the original secretary-treasurer of a corporation, which had failed to designate resident agents, constituted valid service; and it made no difference that the person served was no longer connected in any capacity with the corporation.²³⁸ As a last resort, in the event that none of the corporate officers or adult employees can be located, service may be made upon the Secretary of State or Assistant Secretary of State.

BOOKS, RECORDS, AND ANNUAL REPORTS

The right to information is important to every shareholder. Unless he can apprise himself on corporate affairs, his right to vote becomes a mirage. Every Louisiana Constitution since 1879²³⁹ has imposed an obligation on domestic and foreign corporations doing business in this state to maintain a stock transfer office and to keep books "for public inspection," showing the amount of capital stock subscribed, the ownership and transfers of such stock, its assets and liabilities, and the names and residence of its officers. Our courts have not interpreted the constitutional right of inspection as unqualified or absolute, but have read into it the general common law requirement that the inspection must be at

²³⁶ Service of process upon a local manager was held invalid in *Mouton v. First Nat. Life Ins. Co.*, 177 So. 431 (La. App. 1937). (Applying analogous provision of a statute governing service on domestic insurance companies).

²³⁷ *Frank Melat v. Cooper*, 150 So. 432 (La. App. 1933).

²³⁸ *Holzer Sheet Metal Works Inc. v. Arch Constr. Co. of La.*, 141 So. 872 (La. App. 1932).

²³⁹ La. Const. of 1879, Art. 245; La. Const. of 1898, Art. 273; La. Const. of 1913, Art. 264; La. Const. of 1921, Art. 13, § 4.

a reasonable time for a proper purpose.²⁴⁰ In the early case of *State v. New Orleans Gaslight Company*²⁴¹ Justice Blanchard declared:

“By ‘public inspection’ is meant not the inspection of the idle, the impertinent, or the curious,—those without an interest to subserve or advance or protect. It was never contemplated that any and everybody, as the whim may seize him or them, should be permitted to walk into the office of a company or corporation, and pry into its affairs. But a shareholder or other person with a laudable object to accomplish, or a real and actual interest upon which to predicate his request for information disclosed by the books, is given, by the fundamental law itself, the right to inspect them.”²⁴²

This rule has been repeatedly affirmed, but the courts have been careful to point out that inspection should be denied a shareholder only in exceptional cases, and the burden is upon the corporation to sustain its allegations of improper motive.²⁴³ The right to examine the corporate books is generally upheld and enforced by a writ of mandamus. Also, the shareholder is entitled to dam-

240. For a collection of cases enunciating the general common law rule see 5 Fletcher, Corporations, 575-576, § 2214, n. 23.

241. 49 La. Ann. 1556, 22 So. 815 (1897). Followed in *State v. Dalgarn Constr. Co.*, 168 La. 620, 122 So. 884 (1929); *Orlando v. Reliance Homestead Ass'n*, 171 La. 1027, 132 So. 777 (1930).

242. 49 La. Ann. 1556, 1558, 22 So. 815, 816 (1897). In *State v. Atchafalaya-Teche-Vermillion Co.*, 155 La. 882, 99 So. 633 (1924), the Louisiana Supreme Court held that a creditor with an unliquidated claim against a corporation was not entitled to inspect its books, accounts, and records and that the constitutional provision was primarily for the protection of shareholders and prospective investors. It was pointed out, however, by way of dictum, that a *judgment creditor*, seeking to enforce his rights against shareholders, would be entitled to a writ of mandamus to compel the corporation to permit him to ascertain who the shareholders were and the amount remaining unpaid on their shares.

243. *Orlando v. Reliance Homestead Ass'n*, 171 La. 1027, 132 So. 777 (1930), the shareholder sought to ascertain if the corporation was being mismanaged; *Cockburn v. Union Bank*, 13 La. Ann. 289 (1858), same; *Carey v. Dalgarn Constr. Co.*, 168 La. 620, 122 So. 884 (1930), the owner of one-third of the capital stock was seeking information as to the management and financial condition of the corporation, and as to the net value of his stock; *State v. Bienville Oil Works Co.*, 28 La. Ann. 204 (1876), the stockholder was permitted to examine the corporate books, with the assistance of a competent accountant, to determine how to vote on a proposal for the reduction of capital stock. Cf. *Finance Co. of America at Baltimore v. Brock*, 80 F. (2d) 713 (C.C.A. 5th, 1936) where the stockholders, suing officers and directors for fraudulent misrepresentations, sought a bill of discovery to compel the corporation, not a party to the suit, to produce and permit examination of corporate books and records. Sibley, J., declared (80 F. (2d) 713, 714) that the proposal had “every appearance of a ‘fishing’ enterprise,” since no specific documents were sought; and continued that “The legal remedy for a wrongful refusal is plain and swift, a mandamus.”

ages if he can show injury resulting from a wrongful refusal to allow inspection.²⁴⁴

Section 38, subsection I²⁴⁵ of the Louisiana Business Corporation Act requires every corporation to keep, at its registered office, records of the proceedings of the shareholders and of the directors; and a share register and transfer book showing the ownership of its shares. This provision is supplemented by Act No. 12 of the Third Extra Session of 1934, which requires all corporations to keep books with complete records and accounts of its assets, liabilities, receipts, disbursements, gains, losses, capital, and surplus.²⁴⁶

Subsection III of Section 38, declaring the shareholder's²⁴⁷ right to examine "any and all" corporate books and records, includes the already recognized and defined limitation that the examination shall be at a "reasonable time," and for "proper and reasonable purposes."²⁴⁸ It further safeguards the corporation from officious intermeddling by the definite stipulation that only a shareholder who has been the record holder of at least two percent of the outstanding shares for the past six months shall have the right of inspection.²⁴⁹ It has been suggested that such a requirement would effectually bar shareholders in a large corpora-

244. *Bourdette v. Sieward*, 52 La. Ann. 1333, 27 So. 724 (1900), the plaintiff had been denied an examination of the corporate books, which would have revealed the fact that several large shareholders were selling. As a result he held his stock and bought more. The stock dropped in value and the court held that the plaintiff had an action for damages against the corporate officers.

245. La. Act 250 of 1928, § 38, I, as amended by Act 34 of 1935 (4 E.S.) [Dart's Stats. (1939) § 1118, I].

Subsection II of Section 38 relieves a corporation of the obligation to keep a share register at its registered office in this state, if it keeps such register in some other state and has a transfer agent acting in this state.

246. This statute imposes substantial penalties on a corporation and its officers for failure to keep such records. Regulations of the Secretary of State indicating what is a sufficient compliance with this act are found in its Corporation Handbook, 73-75.

Act 23 of the Third Extra Session of 1934 covers the same ground as, and purports to put teeth in, the constitutional provision already discussed by providing penalties for its violation. See Corporation Handbook, 72.

247. Subsection IV of Section 38 authorizes the corporation to expressly confer the right of inspection upon the holders of bonds or other obligations of the corporation.

248. The advisability of such an express safeguard is indicated by the decision in *State v. Werra Aluminum Foundry Co.*, 173 Wis. 651, 182 N.W. 354 (1921), where a statutory right of inspection was interpreted as absolute, and the motive of the petitioning shareholder was treated as immaterial. Compare, however, the interpretation put on Louisiana's constitutional right of inspection, *supra* note 241. See also Ballantine, *Private Corporations* (1927) 552, with cases collected in notes 168-170.

249. The Michigan statute contains a substantially similar provision,

tion from information,²⁵⁰ but it should be noted that two or more shareholders, whose aggregate holdings equal the required percentage, are authorized to jointly inspect the corporate books. Another query—does the two percentage requirement violate the constitutional right of inspection presently found in Article 13, Section 4, of the Louisiana Constitution of 1921? In the analogous case of *State ex rel. Cotonio v. Italo-American Homestead Ass'n*²⁵¹ Chief Justice O'Niell, speaking for a divided court, limited the constitutional guaranty to a right to inspect those books and records named therein. Thus interpreted, minute books, account books, and certain other records required by Section 38 of the Corporation Act and Act No. 12 of the Third Extra Session of 1934, would not come within its scope. As regards share transfer books and those records clearly within the constitutional mandate, an application of the two percent requirement may well be unconstitutional.

A further limitation on the right of inspection is found in the provision of subsection III that where stock is held by or for a business competitor, or by one who is interested in or holds stock in a competitive business, such shareholder "must own not less than twenty-five percent of stock issued and outstanding for a period of six months before he, or it, can demand the rights and privileges set forth in this paragraph."²⁵² Possibly this requirement will be a trifle hard on the shareholder who is merely "interested" or "holds stock" in a business competitor. Yet stringent rules are necessary in order to curb shareholder blackmail and unfair competition. Again, the objection of unconstitutionality may raise its head.

Mich. Pub. Act 327 of 1931, § 45. The Idaho Act contains a ten percent requirement, Idaho Laws of 1929, c. 262, § 31, Idaho Code Ann. (1932) § 29-143.

Mullens v. Pioneer Gas Co., 154 So. 377 (La. App. 1934) is declaratory of Section 38, III.

250. Rutledge, *supra* note 39, at 332.

251. 177 La. 766, 149 So. 449 (1933), cert. denied 290 U.S. 694, 54 S.Ct. 128, 78 L.Ed. 597 (1933); Note (1933) 8 Tulane L. Rev. 136. The court interpreted Section 64 of Act 140 of 1932, which places all homestead associations under the supervision of the state banking commissioner and provides for inspections by the commissioner, as denying the shareholders in such associations the right to examine minute books, applications for withdrawals, check stub books, and other similar records of such companies. After setting out Article 13, Section 4 of the 1921 Constitution, O'Niell, C. J., declared (177 La. 766, 777, 149 So. 449, 452): "There is nothing in these provisions of the Constitution forbidding the Legislature to curtail the right of a stockholder in a corporation to inspect the corporation's books, other than those which are subject to public inspection. . . ."

252. This probably means that such right of examination is subject to the general limitation that it must be at a reasonable place, and for a reasonable and proper purpose, and that shareholders may cumulate their holdings in order to meet the required percentage.

As an additional measure for the protection and information of shareholders, prospective investors, and creditors, Section 39²⁵³ imposes a duty on the president, or certain other officers of the corporation, to make an annual report to the Secretary of State. Subsection I specifies the facts which must be included therein. Subsection II provides that if such report is not filed within fifteen days after a written request by the Secretary of State, the corporation shall be subject to a penalty of ten dollars for every day of such neglect or refusal. This penalty is hardly sufficient to be effective against a large corporation. The more extreme penalty, in the Michigan and Indiana statutes,²⁵⁴ of forfeiture of the corporate charter for failure to file the report for two successive years, appears entirely justified.

Subsection II further provides that once a year, upon the request of any shareholder of record, the corporation shall send such shareholder a properly verified copy of the last annual report. It has been held that the furnishing of a copy of the annual report is a ministerial duty, enforceable by mandamus.²⁵⁵ Where such statement is not furnished within fifteen days after requested, the statute provides that the shareholder may recover fifty dollars for every day of delay, from the officer or officers charged with the duty of delivering it. Declaring that this penalty provision was enacted "primarily to protect the investing public" and not to penalize the corporate officer who acts in good faith the Louisiana Supreme Court in *Tichenor v. Tichenor*,²⁵⁶ refused to allow recovery of \$4,500 in penalties from a corporation president who mailed an honest and accurate report, but through oversight failed to sign or verify the same.

Section 40²⁵⁷ applies only to those corporations operating pub-

253. La. Act 250 of 1928, § 39 [Dart's Stats. (1939) § 1119]. See also the requirement of annual reports for franchise tax purposes, La. Act 10 of 1935 (E.S.) § 1.

254. Mich. Pub. Act 327 of 1931, § 91; Ind. Stat. Ann. (Burns, 1933) § 25-250. Corresponding Section 36, II, of the Uniform Business Corporation Act provides a penalty of \$50.00 per day for failure to file the annual report. 9 U.L.A. 89 (Perm. ed. 1932).

255. *Tichenor v. Dr. G. H. Tichenor Co.*, 161 So. 198 (La. App. 1935).

256. 190 La. 77, 181 So. 863 (1938), discussed, *Work of the Louisiana Supreme Court* (1939) 1 LOUISIANA LAW REVIEW 314, 405. The court recognized the fact that plaintiff shareholder had obviously refrained from pointing out the technical defect in order to take advantage of the penalty feature of the act. Fournet, J., also stressed the "universally recognized rule of law that statutes imposing penalties must be strictly construed and every doubt must be resolved against the imposition of the penalty." (190 La. 77, 83, 181 So. 863, 864.)

257. La. Act 250 of 1928, § 40 [Dart's Stats. (1939) § 1120]. This provision is not found in the Uniform Business Corporation Act, but is taken verbatim

lic utilities under special or secondary franchises from the state.²⁵⁸ This section requires a statement which shall contain, in addition to the information called for by Section 39, specific figures as to receipts and disbursements. Also, a corporation failing to make such a report is subject to more severe penalties²⁵⁹ than those imposed under Section 39.

CONCLUSION

Sections 41 through 65 govern fundamental changes in the corporate organization or enterprises—voluntary transfer of all corporate assets, amendment of the articles of incorporation, reduction of capital stock, merger and consolidation, proceedings for dissolution, and action by state to vacate the corporate charter. Space limitations have prevented a treatment of these problems in the present article.²⁶⁰

No discussion of the Louisiana Business Corporation Act would be complete without the payment of tribute to those who so carefully and ably drafted this statute.²⁶¹ They have followed the Uniform Business Corporation Act, but have incorporated a number of substantial changes, mostly additions, which have effected a decided improvement. In several instances, however, changes in phraseology were made which were merely the adoption of a preferable and more elaborate mode of expressing the rule of the Uniform Act. It is to be hoped that these variations in expression will not deter our courts from accepting the full benefit of decisions in sister states which have likewise adopted the Uniform Business Corporation Act.²⁶²

from La. Act 267 of 1914, § 22. For a discussion of the requirements of this statute, see *State v. Shreveport Water Works Co.*, 141 La. 1091, 76 So. 210 (1917).

258. *State v. Riverside Irr. Co.*, 142 La. 10, 76 So. 216 (1917), wherein Monroe, C. J., concludes (142 La. 10, 15, 76 So. 210, 218) "that the term 'franchise,' as used in the statute, was intended to be applied to what are called 'secondary franchises,' being special privileges, in addition to the corporate franchise which may be granted by the state (as the right of eminent domain) or by a parish or municipality (as the right to operate a public ferry, or to make use of a street)."

259. The corporation is subject to a penalty of \$250.00 and \$25.00 for each additional day of delay after March 31, the deadline for filing the report.

260. The author plans a companion article, completing the survey of the Louisiana Business Corporation Act.

261. The Joint Committee of the Louisiana State Bar Association and the New Orleans Bar Association which prepared the statute was composed of Charles E. Dunbar, Jr., and Walker B. Spencer, Co-Chairmen, assisted by Charles Rosen, Irving R. Saal, John H. Tucker, Jr., and Rene A. Viosca.

262. La. Act 250 of 1928, § 71 [Dart's Stats. (1939) § 1151] provides, "This Act shall be so interpreted and construed as to effectuate its general purpose to make uniform the law of those states which enact it." (Taken verbatim from Uniform Business Corporation Act, § 76, 9 U.L.A. 105 (Perm. ed. 1932).)