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THE NEW WASHINGTON BUSINESS CORPORATION ACT —RESERVED POWER OF LEGISLATURE TO CHANGE

The new Washington Domestic and Foreign Corporation Act was enacted by the State of Washington at the session of its Legislature convened January 9, and adjourned March 9, 1933.[1] The Act was approved by the Governor on March 21, 1933, and by an express provision therein became effective on and after January 1, 1934.[2] The Act is patterned upon the Uniform Business Corporation Act and may be cited as such.[3] The history of, and the consideration given to, the drafting of this Act is treated in a note introductory to the draft originally submitted to the Legislature, published in an earlier issue of this LAW REVIEW.[4]

Naturally, many and various lines of approach suggest themselves, as the Act in its entirety reflects approximately the entire law of corporations, and the changes made involve policies and problems which for an adequate treatment would require volumes rather than the space allotted here. For example, the new Ohio Corporation Act enacted in 1927 and amended in 1929 has already brought forth three leading articles dealing each with one of the many problems suggested by the Act.[5] Incidentally, it may be observed that the Ohio Act is in many respects quite similar to the Uniform Business Corporation Act, in fact, being enacted after various interchanges of views with the Committee of the Commissioners on Uniform State Laws.[6] Accordingly, the reports of the proceedings leading to the enactment of the Ohio Act furnish much illustrative and enlightening material for the consideration of the

[1] Wash. Laws of 1933, ch. 185.
[2] Section 67.
[3] Section 68.
[4] Uniform Business Corporation Act and The Uniform Stock Transfer Act, 5 Wash. Law Rev. 170 (1930). The only changes as adopted were in sections 21 and 28 (V), where instead of the clause "provisions of the Uniform Stock Transfer Act" there was substituted "the laws of this state." See also handbook of National Conference of Commissioners on Uniform State Laws and Proceedings, 1927, p. 779, and preface to Uniform Business Corporation Act as drafted by the commissioners on Uniform State Laws and approved by the American Bar Association.
[5] DAVIES, "Shares Under the Ohio General Corporation Act," 4 Univ. Cin. L. Rev. 1 (1930) DODD, "Amendment of Corporate Articles Under the New Ohio General Corporation Act," 4 Univ. Cin. L. Rev. 129 (1930) STEVENS, "*Ultra Vires* Transactions Under the New Ohio General Corporation Act," 4 Univ. Cin. L. Rev. 419 (1930).
[6] See HANDBOOK OF UNIFORM STATE LAW COMMISSIONERS, *supra*, p. 781.

Uniform Business Corporation Act.[7] When, with the foregoing, one considers the many recent articles concerning corporate problems forming a background for the recently enacted corporation acts,[8] treating among other subjects the historical development,[9] the changing concepts,[10] the reserved power,[11] and the rights of dissenting stockholders,[12]—it is apparent that it must presently be desirable to limit this consideration of the Washington Act to a summary and somewhat more or less clerical treatment. This will comprise a comparison of the new with the existing law, noting the changes effected, with occasional comments as to the desirability of such changes. It is hoped thereby that later articles may be incited with detailed analysis and consideration which will lead to further improvement in our corporation law

Prefacing this treatment, it is necessary to first consider generally the effect of the new Act upon existing corporations. As to future corporations organized under the Act, it will in the main be necessary to note only the changes from the existing law. As to existing corporations, however, two additional questions are involved first, what provisions of the new Act apply,—a question of construction, and, second, what power has the Legislature to make such changes.

Three provisions in the new Act provide for or suggest limitations as to its application to existing corporations. These provisions are as follows:

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[7] See report of Committees respecting revision of the Ohio Corporation Law and drafts of acts, December 28, 1926.

[8] Particularly the new Ohio and California Acts.

[9] See articles by W S. HOLDSWORTH, English Corporation Law in the 16th and 17th Centuries, 31 Yale L. Jour. 382 (1922) SAMUEL WILLISTON, History of the Law of Business Corporations Before 1800," 2 Harv. L. Rev. 105 (1888), at pp. 111 and 113; DAVIS, Essays in Earlier History of American Corporations (1917) BERLE, Studies in the Law of Corporation Finance (1928). Introductory chapter.

[10] BERLE, Studies in the Law of Corporation Finance (1928) WORMSER, Frankenstein Incorporated (1931) BERLE and MEANS, The Modern Corporation and Private Property (1932).

[11] See STERN, The Limitations of the Power of a State Under a Reserved Right to Amend or Repeal Charters of Incorporation, 53 Am. Law Register I, 73, 145 (1905) DODD, Dissenting Stockholders and Amendments to Corporate Charters, 75 Univ. Pa. L. Rev. 585, 723 (1927) DODD, Amendment of Corporate Articles Under New Ohio General Corporation Act, 4 Univ. Cin. L. Rev. 129 (1930) Note, 31 Col. L. Rev. 1163 (1931) Note, 77 Univ. Pa. L. Rev. 256 (1928) Note, 16 Va. L. Rev. 284 (1930 Note, 14 Corn. L. Quar. 85 (1928) BERLE, Corporate Powers as Powers in Trust, 44 Harv. L. Rev. 1049 (1911) Note, 14 Minn. L. Rev. 413 (1930) RADZINSKI, Power of the Legislature to Alter, Amend or Repeal Charters of Private Corporations, 12 Bi-Monthly L. Rev. 127 (1929).

[12] Note 11, *supra*. LEVY, Rights of Dissenting Shareholders to Appraisal and Payment, 15 Corn. L. Quar. 420 (1930) LATTIN, Remedies of Dissenting Stockholders Under Appraisal Statutes, 45 Harv. L. Rev. 233 (1931) ROBINSON, Dissenting Shareholders: Their Right to Dividends and the Valuation of Their Shares, 32 Col. L. Rev. 60 (1932). The foregoing represent recent leading articles, with extensive citations for a lead in the pursuit of questions sugested.

SECTION 61. Except where otherwise expressly stated herein, this Act shall be applicable to any existing corporation formed under the general incorporation laws of this state for a purpose or purposes for which a corporation might be formed under this Act.

SECTION 62. All acts or parts of acts inconsistent herewith are hereby repealed.

SECTION 63. This Act shall not impair or affect any act done, offense committed or right accruing, accrued or acquired, or liability, penalty, forfeiture or punishment incurred prior to the time this Act takes effect, but the same may be enjoyed, asserted, enforced, prosecuted or inflicted, as fully and to the same extent as if this Act had not been passed.

SECTION 61 provides for the application of the new Act to existing corporations. Note that the only exception here made is where "otherwise expressly stated" in the Act. SECTION 62, repealing Acts inconsistent with the new Act, obviously will change its application to existing corporations so far as they are dependent on the existent inconsistent statutes. SECTION 63 is the saving clause.

It will be interesting to note the comments of the committee which drafted the Ohio Corporation Act on corresponding sections.[13] With respect to the section of their Act relating to application to existing corporations, which is similar to SECTION 61, *supra*, they say

> "Existing corporations which continue to exercise their franchise will automatically come under and be subject to this Act. All statutory proceedings or action of such corporations must be taken and done in accordance with this Act. The rights of shareholders, as between themselves, as expressed in existing articles of incorporation or in preferred stock, are, of course, saved by the saving clause."

With respect to the section providing a saving clause, which is identical with SECTION 63, *supra*, they say

> "This section is taken from the New York General Corporation Law (Section 17, L. 1923, ch. 732) It is the belief of the committee that this carefully phrased clause more effectively covers all of the rights, liabilities and interests than any saving clause which has come to its attention."

Notwithstanding this statement the rights protected by the saving clause are not defined. The state may exercise its police power[14] and we still have to reckon with the reserved

[13] See note 7, *supra*, pp. 148, 149.

[14] The Dartmouth College Case, 4 Wheat, 518 (U. S. 1819) holding that the charter of a corporation is a contract, has no application to the exercise of the police power for the health, safety, and general welfare of the community, since these are incidents of sovereignty which the state cannot release. *Beer Co. v. Mass.*, 97 U. S. 25 (1878).

power clause, whereby the Legislature is empowered to alter amend, or repeal all laws pertaining to corporations. The rights contemplated by the statute may be those involved between the state and the corporation alone, may be those involved between the corporation and shareholders, may be those involved among the shareholders alone, or may be those which while primarily between the state and the corporation evidently affect the shareholders.[15] In fact, it may be questioned whether any reserved power, if exercised, does not affect shareholders' prior rights.[16] It is generally conceded that the state may make changes designed for the benefit and protection of the public, and it is submitted that such regulations would apply to existing as well as to future corporations. It may also be urged as a matter of principle with some supporting authority that intra corporate regulations, and even matters *inter sese* among shareholders, are in many instances of such public concern that they may be similarly considered.[17] If so, the interests of uniformity in the administration of the law, and the necessity for advantageous competition of existing corporations with corporations formed under the new Act, would seem to require that in all cases unless clearly inapplicable because of their nature,

[15] Mr. Cades writes to this effect in a note in 77 Univ. Pa. L. Rev. 256 (1928) at p. 258: "When the power is reserved by the state to repeal, alter or amend it is clear that some of the amenities of the association are destroyed, but that there still remains some limitation on the power of the state to amend the corporatin laws. The effect of such a reservation of power by the state on the immunity from impairment of the relations of the shareholders *inter se* is not clear. Many authorities seem to proceed on the theory that the creation of the relations as to shareholders *inter se* is a matter separate and distinct from the creation of the relations between the corporation and the state, and that therefore the state may not directly alter any of the relations of the shareholders *inter se*. Other authorities would seem to lend color to an opposed theory. According to the latter view, all the terms of the agreement between shareholders, as to the management of the corporation and as to their interest in the corporation, are conditions upon which the state grants the privilege of corporate existence. The reserved power gives the state the absolute power to withhold or alter this privilege." He continues, "No case carries this theory to its logical conclusion." (Authorities cited.)

[16] Mr. Fuller in a note in 14 Corn. L. Quar. 85 (1928) at p. 86 says: "It is argued, therefore, that under the reserved power, the state can change only the rights existing between the corporation and the state, and cannot alter rights of the shareholders *inter sese*. This reasoning has not been strictly followed and many amendments have been upheld that do seem to affect rights existing between the shareholders themselves. This is a result of the theory that the shareholders have impliedly consented to amendment by becoming members of a corporation whose contract with the state they knew was subject to the state's reserved power to amend. Furthermore, it is difficult for us to see how the state could, in any case alter a charter without in some way effecting a change in the original plan of the shareholders. The courts' answer to these arguments is that an amendment is constitutional if it does not work a fundamental change in the nature of the business or infringe on vested rights." (Authorities cited.)

[17] See Note, 31 Col. L. Rev. 1163 (1931) Note, 16 Va. L. Rev. 282 (1930) Dodd, Amendment of Corporate Articles under the New Ohio General Corporation Act, 4 Univ. Cin. L. Rev. 129 (1930), at pp. 156, 157.

or because of interference with vested rights or property interests, the provisions of the new Act should apply What rights of shareholders will be protected and are therefore not subject to the new Act, is still a matter of some doubt. As the saving clause undertakes no specific recital of these rights, it is safe to say that they will be determined as a matter of judicial decision, and as their determination is so closely allied with that power of the state to change the law, further discussion will be deferred to the consideration of that question.

The *Dartmouth College Case*[18] was decided by the Supreme Court of the United States in 1819. This case held that the charter granted was a contract within the meaning of the Constitution of the United States declaring that no state shall pass any law impairing the obligation of contracts. It has since been questioned whether a charter is a contract between the state and either the corporation or incorporators.[19] It is certainly not within the modern concept of a contract. It is also questioned whether it is even a franchise, it being urged that under our present general corporation laws it is to be conceived of merely as a group of natural persons voluntarily associated under a contract for the conduct of business, regulated by statute.[20] It is not within the scope of this article to discuss these questions, but they are relevant to the determination of the power of the state to alter, amend, or repeal the corporate charters or laws relating to corporations.

Notwithstanding the doubts expressed as to the soundness of the decision expressed in the *Dartmouth College Case,* the Supreme Court of the United States has adhered to it in later cases. The states, alarmed at the possibility of private corporations becoming uncontrolled, either through their constitutions, statutes, or articles, reserved the power to alter, amend, and repeal. The Constitution of the State of Washington provides that.

> "All laws relating to corporations may be altered, amended, or repealed by the Legislature at any time, and all corporations doing business in this state may, as to such business, be regulated, limited, or restrained by law."

Just what was intended to be covered by this clause has been questioned.[21] It is contended that the state can change only the

[18] *Trustees of Dartmouth College v. Woodward,* note 14, *supra.* See BALLANTINE, PRIVATE CORPORATIONS, (1st Ed., 1927), at pp. 809, 811.

[19] See BALLANTINE, PRIVATE CORPORATIONS, (1st Ed., 1927), at p. 810; DOE, A New View of the Dartmouth College Case, 6 Harv. L. Rev. 161 (1892) DODD, Dissenting Stockholders and Amendments to Corporate Charters, 75 Univ. Pa. L. Rev. 585 (1927) at pp. 593-595.

[20] See note 19, *supra.* Also see DODD, Dogma and Practice in the Law of Associations, 42 Harv. L. Rev. 977 (1929).

[21] See notes 15 and 16, *supra.* BALLANTINE, PRIVATE CORPORATIONS (1st Ed., 1927), chapter XXI.

rights existing between the state and the corporation, and cannot alter the rights of the shareholders *inter sese*. It is so contended both from the viewpoint that the Legislature in making a reservation intended only to reserve the power to amend its own grant, and that it could not apply to the contract between the corporation and shareholders, as this would impair the contractual relation of the stockholders *inter sese*. While this view has received some support, it has not been generally followed.[22] It is argued that many provisions concerning the internal management of corporations are of public interest and are conditions to the exercise of the corporate franchise, again the stockholders may be said to have consented to the modifications of their agreements by becoming members of a corporation whose contract with the state they knew was subject to the state's reserved power to amend.

There is considerable confusion in the authorities not only in traditional formulae but in a failure to appreciate the nature of the rights and interests concerned. It is quite commonly stated that no fundamental change can be made in the nature of the business, again that voting rights may not be changed, and still again that property interests may not be affected with or without compensation. It may first be noted that many changes that are enacted might well come under the police power;[23] that changes where there is compensation are in their nature at least similar to the exercise of eminent domain;[24] that the consent to be implied in the reserved power to make changes is that which would undoubtedly be protected by equitable limitations.[25] Any change, even though limited to the contract between the state and incorporators, to a cer-

[22] This is the contention of Judge Stern in his article cited in note 11, *supra*. For cases supporting this view see Note, 77 Univ. Pa. L. Rev. 256 (1928), note 12.

[23] See Note, 31 Col. L. Rev. 1163 (1931) at p. 1164, where it is stated that: "Most changes imposed by the states in the relationship between the corporation and the general public have been of the same nature as those enacted under the police power. When the wisdom of some restraint on the state's right of alteration under the reserved power appeared, the same tests of due process were applied. The reserved power and the police power tend, therefore, insofar as changes affecting the general public are concerned, to coalesce. Virtually all of the regulations justified by the courts under the reserved power might well have been sustained under the police power without reference to the additional control over corporations. (Cases cited.)" See also, Dodd, Amendment of Corporate Articles under the New Ohio General Corporation Act, 4 Univ. Cin. L. Rev. 129 (1930), at pp. 154-157.

[24] See Note, 14 Corn. L. Quar. 85 (1928) at 88, where Mr. Fuller states that: "Furthermore, since there is intimation in the cases that there is an element of public interest involved, this element of public interest plus compensation to reduce the rigor of its effect, might be treated as validating such amendments as a sort of eminent domain." Dodd, Amendment of Corporate Articles under the New Ohio General Corporation Act (1930), at page 164.

[25] Berle, Corporate Powers as Powers in Trust, 44 Harv. L. Rev. 1049 (1931) at p. 1066, Note, 77 Univ. Pa. L. Rev. 256 (1928).

tain extent affects the rights *inter se* among the shareholders. The interest of the state in the corporation of today should perhaps not be limited to the contract interests as involved among a small group of shareholders. It has been urged that the private corporation has become an institution.[26] The exercise of the police powers is ever developing, and the state's interest in this so-called institution may be that which should be exercised either as a police power or through powers analogous to the exercise of eminent domain. Equitable limitations suggest that the reserve power of the corporation to amend its charter must be so exercised that the result will tend to benefit the corporation as a whole, and that the benefit or sacrifice shall be distributed between the shareholders or classes proportionately or ratably at least as their interests appear. If not, and one must sacrifice at the expense of another, there should be compensation, the justification for which will be found in the benefit to the corporation as a whole, in turn justified by the interest of the state in the welfare of the corporation as a matter of public concern. Difficulties, however, will continue to be encountered until there is a recognition of the distinction between the policies involved in treating with a closed corporation, composed of a few individuals, and a large corporation, composed of an investing general public, who are primarily interested from an investment standpoint.

Briefly summarizing, the traditional objections to the exercise of the reserved power are that the obligation in the contract of the shareholders *inter sese* is impaired, that these are matters in which the state is not concerned, and that the due process clause protects the property rights which include arbitrary discrimination. On the other hand, it is stated that by the reservation clause the state has expressly reserved the right to regulate and control the corporation as a matter of public concern, that having created the corporation, it has the authority to make such changes as it sees fit, that the shareholders have impliedly consented to the reservation and the exercise of reasonable powers thereunder, that in any event if the powers exercised are for the general welfare of the corporation they may be justified as an extension of the police power, or if provision is necessitated for compensation they may be justified as analogous to the exercise of eminent domain. In any

[26] See BERLE and MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (1932). The authors assert that the American corporation has ceased to be a private business device, and has become an institution. Professor Robert S. Stevens in a recent book review, 18 Corn. L. Quar. 634 (1933), states that this volume is the most comprehensive and illuminating exposition of the modern corporate system that has been published. See also DODD, Amendment of Corporate Articles under the New Ohio General Corporation Act, 4 Univ. Cin. L. Rev. 129 (1930), at pp. 130, 131.

event, a study of the decisions will show an increasing tendency to recognize the reserve power. One writer states that the vested right has varied directly with the practical importance of the interest destroyed by the alteration, and inversely with the advantage of a change.[27] It is a safe observation that so far as the reserve powers exercised are not arbitrary, are essential to the welfare of the corporation, and substantially protect the interests of the parties concerned, that the courts will find reasons to justify such powers when exercised. It is submitted that the powers exercised in the new Washington Act will be sustained.

In the following treatment the sections of the Act as adopted in Washington will be considered in turn. No attempt has been made to exhaust the authorities either in the State of Washington or elsewhere.[28]

SECTION 1 deals with definitions. These conform to general usage except that it should be noted Subsection 7 provides that a "subscriber becomes a shareholder upon the allotment of shares to him," and Subsection 9 provides that " 'allotment' means the apportioning of a certain number of shares to a subscriber in response to the application contained in his subscription, or to a shareholder pursuant to the declaration of a stock dividend. The allotment of shares to the incorporators, or to persons whose subscriptions were approved by the incorporators before incorporation and were unrevoked at the time of incorporation, shall be considered automatically coincident with incorporation." It will be seen that the controversial question of when a subscriber becomes a shareholder is settled, being fixed as of the time of allotment of shares without the necessity of notice or other acceptance, and that as to subscriptions prior to incorporation, the allotment is automatically coincident with the incorporation. Subsection 10 in defining capital stock of a corporation makes this term definite and specifically includes the aggregate of cash, and value of any other consideration rendered as payment of allotted shares having no par value. This should be contrasted with the prior existing statute which in providing for the reduction of capital stock excludes so much of the capital stock as is represented by non par value stock. This will be considered subsequently under Section 40 of the new Act relating to the reduction of capital stock.

SECTION 2 deals with the purpose of incorporation and the qualifications of incorporators. The new Act requires "three or more

[27] See Note, 31 Col. L. Rev. 1163 (1931).

[28] The sections of the Washington Act are for the greater part identical with the sections of the Uniform Business Corporation Act. The explanatory notes of the commissioners follow many of the sections. See Vol. 9, Uniform Laws Annotated, p. 27 *et sequa.*

natural persons of full age, at least two-thirds of whom are citizens of the United States or its territories." The minimum number of incorporators under the old act was two. The specific recital of the qualifications suggests their recital in the articles of incorporation.[29]

SECTION 3 provides for the articles of incorporation. These changes should be noted.

(1) Acknowledgement by three of the incorporators instead of all,
(2) The name must include abbreviation "Inc." or "Corporation" or "Incorporated" or "Company" or abbreviation "Co." If "Company" or "Co" are used, the word or the abbreviation must not be immediately preceded by the word "and" or the abbreviation "&;"
(3) The duration may be permanent instead of being limited to fifty years,
(4) The post office address is required of the registered office instead of the location of the principal place of business,
(5) A statement is required as to the authorized number of par value shares and the par value of each share, and if any of these shares have no par value, the authorized number of such shares as contrasted with the former law which required the statement as to the amount of its capital stock, or if non par value, the amount of its initial non par capital.
(6) A description of the classes of shares, the number in each class, and their relative rights, voting power, preferences, and restrictions, as contrasted with no requirement under the previous statute,
(7) The paid in capital with which the corporation will begin business. There was no such provision under the old law,
(8) The first directors with their post office addresses with no fixed term of office. Under the old law post office addresses were not required, while the term of office was limited from two to six months,
(9) The post office address of the incorporators and a statement of the number of shares subscribed by each which shall not be less than one and the class of shares for which each subscribed. The prior law contained no such requirement.

The substantial rather than the formal changes to be noted in the foregoing are those requiring the articles to set forth the classes and restrictions of shares mentioned in (6), supra. This calls for a financial plan of the corporation prior to the filing of the articles, unless it is to be accomplished later by amendment.

[29] O'BRYAN and OWENS, WASHINGTON FORM BOOK (1st Ed., 1932), p. 949.

The other substantial change is in (9), supra, requiring the incorporators to be subscribers, and to state the number of shares subscribed by each.

SECTION 4 provides limitations for the use of the corporate name. The right of the legislature to change the corporate name has been passed upon in this State, at least when being exercised for the protection of the public.[30] The provision in Subsection 1 requiring new corporations to include the abbreviations "Inc." or "Co.", or the words "Corporation" or "Incorporated" is clearly an exercise of such power. It is expressly provided that this subsection shall not apply to existing corporations. Subsection 2 prohibits the use of deceptively similar names and does not change the exisiting law It provides that a corporation about to change its name or ceasing to do business may consent to the use of a deceptively similar name.[31] Subsections 3 and 4 are new provisions providing for protection of names for corporations to be filed in the future. Subsection 8 provides expressly that the unlawful assumption of a corporate name shall not vitiate corporate existence, and that notwithstanding the issue of the certificate of incorporation, the use of an unlawful name may be collaterally attacked. It may be observed that this section does not change the former law, which permits the adoption of the name of a delinquent corporation.[32]

SECTION 5 requires that the triplicate originals of the articles of incorporation shall be delivered to the Secretary of State. An endorsement of his approval is to be placed on each, one is to be retained and recorded, the other two are to be returned to the incorporators, one to be filed for record in the office of the auditor, the other to be retained by the corporation. Upon approval of the articles and the payment of all costs, the Secretary of State will issue a certificate of incorporation, and upon its issue the corporate existence begins. Outside of the procedural changes necessitated by the expressed policy of insuring authentic articles, this section is important in that it definitely fixes the time of the beginning of corporate existence. It also provides that upon the issuance of the certificate of incorporation, prior subscribers become shareholders.[33]

SECTION 6 deals with subscriptions for shares before incorporation. It provides that such subscriptions shall be irrevocable for

[30] *Union Trust Co. v. L. H. Moore*, 104 Wash. 50, 175 Pac. 565 (1918).

[31] This conforms with the practice of the Secretary of State, although there was a technical difficulty as long as the former corporation law exists.

[32] See Wash. Rem. Rev Stats., 1933, sec. 3847.

[33] See 9 Uniform Laws Annotated, p. 48. Commissioners' notes.

a period of one year except upon such grounds as will permit the rescission of any contract. It further provides that such subscriptions shall be revocable after one year unless prior to such revocation a certificate of incorporation is issued. Subscriptions for shares may be enforced according to their terms, and when no provision as to the time of payment is made, the shares shall be paid for on the call of the board of directors. The provision making these subscriptions irrevocable except for fraud, duress, or undue influence in their procurement, settles an irreconcilable conflict of authority and changes the former law of this State. The new provision seems desirable as in accord with public interest that the new corporation should have as resources enforceable subscriptions if fairly obtained.

SECTION 7 provides that the minimum amount of "paid-in" capital with which a corporation may begin business shall not be less than $500.00.

SECTION 8 imposes certain conditions precedent to the beginning of business and provides a penalty for their violation. These conditions are: (a) filing the articles for record in the office of the county auditor; (b) the payment to the corporation of the "paid-in" capital with which it may begin business, and (c) the filing with the county auditor of an affidavit by a majority of the directors, stating the amount of "paid-in" capital with which it will commence business and that it has actually been paid to the corporation. To insure compliance with these conditions, it is further provided that the officers and directors who fail to dissent if any of these conditions are violated shall be liable for the debts or liabilities arising therefrom. The penalty will protect the creditors in the event of noncompliance. This section definitely establishes the requirements mentioned as conditions precedent to beginning business rather than as conditions precedent to corporate existence. It should be noted that Subsection 1 by implication permits debts and transaction of business incidental, and therefore prior to the organization of the corporation, or the obtaining of subscriptions, or the payment for shares.[34]

SECTION 9 provides that the certificate of incorporation issued by the Secretary of State shall be conclusive evidence of the fact

[34] The promoters of a corporation are personally liable upon contracts made by them before incorporation, and by the weight of authority for services and expenses in the organization of a corporation. Some states held the corporation liable for services and expenses necessarily incurred in its organization, but the weight of authority requires definite approval by the corporation after its organization unless such liability is imposed by its charter or by general law. BALLANTINE, CORPORATIONS (1st Ed.), 1927, secs. 47a and 48. The implication in subsec. 1 suggests the necessity for an express understanding providing for the liability for such charges.

of incorporation, but that the State may dissolve corporations which should not have been formed under the Act, or shall have been formed without compliance with prescribed conditions precedent to incorporation. This section does not alter the present law by which the State may question corporate existence when conditions precedent to incorporation have not been substantially complied with. On the other hand, it does change the law with respect to *de facto* existence by prescribing that the certificate issued by the Secretary of State shall be conclusive. This will settle a controversial and much litigated question.[35] It does not necessarily provide an exclusive test and still leaves room for the question of a corporation by estoppel.

SECTION 10 specifies the purpose and effect of filing or recording papers required to be filed. It provides that the purpose is to afford the public the opportunity of acquiring knowledge of the contents of such papers, but that no person dealing with the corporation shall be charged with constructive notice thereof. It will be seen that this provision is for the protection of the public rather than for the protection of the shareholders. Filing as constructive notice was occasionally resorted to for the purpose of showing an ultra vires contract.

SECTION 11 distinguishes corporate capacity from corporate authority and provides specifically certain powers that every corporation shall possess. It provides in Subsection 1 that the corporation shall have the capacity to act possessed by natural persons. In so doing, it recognizes the difference between power and right to act, and makes the law speak the truth, for a corporation *can* commit an unauthorized act. This should do away with much of the confusion heretofore existing because of the reluctance of some courts to recognize this fact. It abolishes the limited corporate capacity doctrine and makes room for the development of a general capacity doctrine based upon the principles of the laws of agency.[36] This provision, with *Section* 10 *supra* which abolishes the doctrine of constructive notice, will remove the two sources of greatest confusion in the ultra vires cases.

The corporate powers enumerated in Subsection 2 are those that are essential or usually essential to the conduct of business by any corporation. They conform quite generally with the law elsewhere, and with the law of this State except that paragraph "b" of this subsection permits perpetual existence. Our law has heretofore limited corporate existence to fifty years. Some question may be

[35] See extensive note by Commissioners in 9 Uniform Laws Annotated 52.

[36] See 9 Uniform Laws Annotated, pp. 57-62, Commissioners' notes.

raised as to the extension of charters when their time of existence is once fixed,[37] although the power was expressly conferred by a former act of our legislature, and seems never to have been questioned.

SECTION 12 provides for holding shares and securities of other corporations. It is in accord with our present law.

SECTION 13 provides that the shares of a corporation may be divided into classes with such rights, voting power, preferences and restrictions as may be provided for in the articles of incorporation. The only stock provided by former statutes of this State include par, non par, common, and preferred stock.[38] The only provision made for different classes was in the preferred stock, and apparently only preferred stock could be issued with limited or no voting power.[39] The new section seems desirable in permitting greater variation in the form of investment and enterprise. On the other hand, sufficient protection seems to be afforded to the investor by the various information required to be filed or recorded, the fiduciary obligation placed upon the management, and the notice directly afforded the purchaser of such shares, apprising him of the terms and exact nature of his investment.[40]

SECTION 14 outlines information required to be specified in the stock certificate and provides for the issue of share warrants. The total number of the authorized par value and non par value shares, and the rights, voting powers, preferences and restrictions granted to or imposed upon the shares of each class and a summary thereof with reference to the articles of incorporation when more than one class is issued must be stated in the certificate. The intent and purpose of such provisions are obvious. It should be noted that shares cannot be listed on the New York stock exchange unless the "certificates of every class recite the preferences of all classes." Subsection 4 provides for the issue of share warrants pursuant to the resolution of the board of directors.

SECTION 15 provides for the allotment of shares and their consideration. Subscriptions for shares having a par value shall be

[37] Art. 12, Sec. 5, of the Constitution of the State of Washington provides that: "The legislature shall not extend any franchise or charter, nor remit the forfeiture of any franchise or charter of any corporation now existing, or which shall hereafter exist under the laws of this state." As this provision by its terms applies only to the extension of charters, it contemplates, if anything, charters with a fixed term of duration and will not apply to charters having a perpetual existence. It is interesting to note that Wash. Rem. Rev. Stats. of 1933, sec. 3805, provides that, "If the articles of incorporation of any corporation state a time of existence less than fifty years, its time of existence may be extended by amendment but not beyond a period of fifty years from the date of its incorporation." This statute seems never to have been questioned.

[38] Wash. Rem. Rev. Stats. of 1933, sec. 3805 and sec. 3812.

[39] Wash. Rem. Rev. Stats. of 1933, sec. 3812.

[40] These provisions will be discussed under the appropriate sections.

paid for either with cash or with other consideration at a fair valuation. Subscriptions for shares having no par value if signed before incorporation shall be paid for as determined by the incorporators, if signed after incorporation, they shall be paid for as determined by the shareholders or by the board of directors under authority conferred by the shareholders or articles.

SECTION 16 provides that certificates of stock shall not be issued until the shares represented thereby have been fully paid for. This applies also to shares allotted as stock dividends. A note or uncertified check will not be deemed payment until the note or check has been paid. This section will obviously do away with the many problems heretofore arising by reason of the transfer of stock which had not been paid for.

SECTION 17 provides for the valuation of consideration for shares. The valuation placed by the incorporators, the shareholders, or the directors, as the case may be, upon consideration other than cash will be conclusive as to the obligation of the shareholder to the corporation. The same is true with respect to surplus transferred to capital as payment for shares allotted as stock dividends. This does not contemplate an arbitrary valuation. Subsection 4 of article 20 *infra* expressly reserves rights of any person under the common law or principle of equity against an incorporator, subscriber, shareholder, director, officer or the corporation because of any fraud practiced upon him.

SECTION 18 provides for the filing of a report with an affidavit as to the consideration received or to be received in payment for shares allotted. It also provides the penalty for failure to file. Such reports, duly verified, must be filed within thirty days after incorporation and additional reports must be filed within ninety days after every subsequent allotment of shares and must contain a statement of the number of shares allotted to the date of the report, an accurate, detailed and itemized description of the consideration received or to be received for the same, and a statement of the valuation upon any consideration other than cash received or to be received in payment. The purpose of this section undoubtedly is to afford those interested the opportunity not only to ascertain the stated capital stock but to scrutinize the consideration which actually entered into its make-up. While it is somewhat doubtful whether creditors actually do rely upon the capital stock of a corporation, this provision at least affords them a reasonable opportunity to judge the value of the assets if they so desire. The fact that notice is given those who are interested in securing the same, perhaps justifies the provision in *Section* 17 that the valuation placed upon the consideration shall be conclu-

sive. The severity of the penalty provided should secure strict compliance.[41]

SECTION 19 is to the effect that shares allotted in violation of, or without full compliance with the provisions of the Act, shall not make the shares so allotted invalid. Some question may be raised as to whether this provision is advisable where an allotment of shares is made in excess of the number authorized by the articles. It may well be contended that this will vary the contract rights of the existing shareholders, and that the balance of convenience will be better served by restricting the holder of such shares to an action for damages against the corporation. Such has been the law in the similar situation where the corporation has reissued shares upon the surrender of a forged certificate and these shares have come into the hands of an innocent purchaser for value.[42]*

LESLIE J AYER.**

[41] This is one of the most important requirements in the new act. A similar requirement in the Ohio Act was recommended as one of the outstanding merits of that act. It is believed that the law should concentrate the attention of the creditor upon the actual assets and refuse to support a supposed reliance upon the aggregate par value. See commissioner's note, 9 Uniform Laws Annotated, pp. 70, 71. COOK, "Water Stock"—Commissions—"Blue Sky Laws"—Stock Withut Par Value, 19 Mich. L. Rev. 583 (1921).

[42] BALLANTINE, CORPORATIONS (1st Ed.), 1927, sec. 151.

*To be continued.

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