Michigan Law Review

Volume 55 | Issue 3

1957

Corporations - Ultra Vires Act - Effectiveness of Action by Informal Meeting of Board of Directors

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CORPORATIONS—ULTRA VIRES ACT—EFFECTIVENESS OF ACTION BY INFORMAL MEETING OF BOARD OF DIRECTORS—Defendant insurance company issued a policy on the life of the president of plaintiff corporation with the corporation named as beneficiary. The president, his wife in the capacity of secretary-treasurer, and son were the sole stockholders of the corporation. Pursuant to a divorce agreement between the president and his wife, a part of the insurance policy was assigned to the wife at an informal board of directors' meeting with the concurrence of the wife and son. The president died and his stock was sold to the present stockholders. The corporation

then sued the insurance company to collect the full amount of the insurance policy, declaring that the previous assignment was void. Defendant, having already paid the wife her share as prescribed by law,[1] contended that it could not be required to pay again to the corporation the amount which it had already paid. At the time of the assignment, the corporation was apparently solvent and up to the time of the trial no existing or subsequent creditor had objected to the assignment. The district court entered a decree for the corporation. On appeal, *held,* reversed. Plaintiff corporation and the new stockholders claiming through the deceased president are estopped to deny the validity of the assignment executed at the informal board of directors meeting. *Philadelphia Life Ins. Co. v. Crosland-Cullen Co.,* (4th Cir. 1956) 234 F. (2d) 780.

As a general rule, directors can bind a corporation only when they act as a board at a legal meeting.[2] According to many modern authorities, however, consent of all the stockholders to corporate conveyances and gifts will bind the corporation even though made at an informal meeting for non-corporate purposes.[3] The court in the principal case recognized the validity of this informal corporate approval, relying principally upon two theories. First, the court held that the corporate entity will be ignored when the interests of justice require. On numerous occasions, other courts have so held.[4] Although the result in a particular case may be desirable, this approach is open to question, for once the corporate entity is overlooked, further problems may arise.[5] The second and sounder theory advanced by the court[6] is that ratification at an informal meeting where all

1 N.C. Gen. Stat. (1950) §§58-205, 58-206.

2 Tuttle v. Junior Building Corp., 228 N.C. 507, 46 S.E. (2d) 313 (1948); O'Neal v. Wake County, 196 N.C. 184, 145 S.E. 28 (1928); BALLANTINE, CORPORATIONS, rev. ed., §44 (1946).

3 Whitwell v. Henry, (Ark. 1956) 286 S.W. (2d) 852; Bergman Drive-In v. Houston Sash and Door Co., (Tex. Civ. App. 1953) 256 S.W. (2d) 661. See DORIS AND FREEDMAN, CORPORATE MEETINGS, MINUTES, AND RESOLUTIONS, 3d ed., 133 (1951).

4 Park Terrace, Inc. v. Phoenix Indemnity Co., 241 N.C. 473, 85 S.E. (2d) 677 (1955), noted in 34 N.C. L. REV. 531 (1956), quoted extensively in the principal case, held the court will *automatically* ignore the separate corporate existence if it is owned by one man. *Accord:* Metropolitan Holding Co. v. Snyder, (8th Cir. 1935) 79 F. (2d) 263; Komow v. Simplex Cloth-Cutting Machine Co., 109 Misc. 358, 179 N.Y.S. 682 (1919), affd. 191 App. Div. 884, 180 N.Y.S. 942 (1920), takes the unique position that since all the parties to the agreement owned all the stock of the corporation, they were in the relation of partners.

5 For example, the courts must decide whether the income of the corporation is to be taxed as the income of the individual stockholder and whether the debts of the corporation are to be considered the debts of the individual stockholders. The Supreme Court of the United States recognized these difficulties when it limited its application of this theory to those exceptional situations where recognizing the corporate entity would prevent adequate protection of public or private rights. New Colonial Ice Co. v. Helvering, 292 U.S. 435 at 442 (1934). See generally, "Disregarding corporate existence," 34 A.L.R. 597 (1925).

6 This view assumes that the rights of creditors are not prejudiced. Since the theory arose to achieve justice in a particular case, it would not be applicable if its application would be detrimental to third parties.

the stockholders are present constitutes adequate corporate approval.[7] In addition to being consistent with accepted legal principles in recognizing the separate corporate existence, this solution eliminates the problems implicit in the first theory. Since the general rule requiring approval at a formal meeting is for the benefit of the stockholders, i.e., to assure them of thoughtful action, they should be able to waive the formal requirements.[8] If all the stockholders concur in the waiver, there can be no justification for a plea of *ultra vires* on the part of the stockholders or the corporation.[9] The instant decision, estopping the stockholders who received their interests from the president from asserting a position inconsistent with prior unanimous stockholder approval follows logically from the legal principle that an informal board of directors meeting is binding on the corporation.[10] This case is indicative of a desirable trend in the law toward resolution of the conflict between the formal requirements necessary for corporate action and the informal manner in which stockholders frequently conduct the business. It is hoped the courts will not complicate the movement by becoming needlessly involved with the problems inherent in ignoring the corporate entity when the simpler theory offers an equally desirable solution.

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[7] Bulger v. Colonial House of Flushing, 281 App. Div. 847, 119 N.Y.S. (2d) 233 (1953). Lake Park Development Co. v. Paul Steenberg Construction Co., 201 Minn. 396, 276 N.W. 651 (1937), on facts are quite similar to the principal case held the stockholders may even invest the officers with power to perform ultra vires acts or to appropriate corporate assets to non-corporate purposes.

[8] MacQueen v. Dollar Savings Bank Co., 133 Ohio St. 579, 15 N.E. (2d) 529 (1938); People v. North River Sugar Refining Co., 121 N.Y. 582, 24 N.E. 834 (1890).

[9] Temple Enterprises v. Combs, 164 Ore. 133, 100 P. (2d) 613 (1940).

[10] Thompson v. M. K. & T. Oil Co., 5 Cal. App. (2d) 117, 42 P. (2d) 374 (1935); Merchants and Farmers Bank v. Harris Lumber Co., 103 Ark. 283, 146 S.W. 508 (1912).