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THE CORPORATE PARTNER

By SCOTT ROWLEY*

THE problem relating to the power of a corporation to enter into a partnership or to subject itself to partnership rights and liabilities with an association or an individual becomes of increasing importance as the number of corporations becomes greater and as business technique becomes more involved. At times it may become acute.

It is a generally conceded principle of corporation law that a corporation has such powers, and such powers only, as are given to it by the state. These rights may be given expressly or by necessary implication.¹ If, then, the corporation may be a partner, this power does not accrue by reason of an inherent right to be a partner, but by reason of a particular grant, expressly or impliedly given by sovereign authority. There being nothing inherently illegal² in such a relation, it is clear that this right, if not prohibited by constitutional limitations, may be granted by legislative action. This principle is recognized and approved in the Uniform Partnership Act.³

The only obstacle to corporate capacity for the partnership relation is the principle of *ultra vires*. No difficulty is encountered when a constitutional statute expressly and unambiguously meets the situation. If such a statute expressly authorizes corporations to enter into partnerships which promote their general purposes, such a relation is clearly permissible.⁴ If, on the other hand, such a statute expressly forbids such a relation, then it

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¹Central Transp. Co. v. Pullman Palace Car Co., (1891) 139 U. S. 24, 11 Sup. Ct. 478, 35 L. Ed. 55; Converse v. Emerson, T. & Co., (1909) 242 Ill. 619, 90 N. E. 269; Atty. Gen. v. N. Y. N. H. & H. Ry., (1908) 197 Mass. 194, 83 N. E. 408; Schwab v. E. G. Potter Co., (1909) 194 N. Y. 409, 87 N. E. 670.

²Hackett v. Multnomah Ry., (1885) 12 Or. 124, 6 Pac. 659; New-Reg. Co. v. Rockingham Pub. Co., (1915) 118 Va. 140, 86 S. E. 874.

³Sec. 2, cl. 1 and 3. "In this Act. . . 'Person' includes individuals, partnerships, corporations and other associations." Sec. 6, cl. 1. "A partnership is an association of two or more persons to carry on as co-owners a business for profit."

⁴Butler v. Am. Toy Co., (1878) 46 Conn. 136; Breinig v. Sparrow, (1907) 39 Ind. App. 455, 80 N. E. 37.

is apparent that no attempt to establish such a relation can be effectual.⁵ In either case the result is certain.

The real difficulties, both theoretically and factually, occur in one of two ways. First, when the statutes do not expressly authorize or forbid such a relation, thus raising the question of implied authority. Second, when, by statute or by judicial decision, corporate power to enter a partnership is forbidden, but, having been attempted, the rights and liabilities of the corporation in the partnership affairs are involved, not as a partner, but under other bases of rights and liabilities.

In the first problem, where the statutes do not expressly provide for the situation, there are two possible arguments favoring denial of the power. The first is, that the partnership relation is so foreign to the nature and general customs of corporations that it is not to be presumed to be necessary to the carrying out of the express powers of the corporation, that a partnership and a corporation are incongruous.⁶ This reason does not seem convincing. It may show that, as a rule, a corporation may not find a partnership relation necessary to carry out successfully the objects of its incorporation: but, after all, the necessity and congruity are, in reality, matters for factual determination, under the particular circumstances of each case. The tendency of the courts is to enlarge rather than to restrict the scope of implied powers.⁷

A much more difficult problem presents itself when the questions of legislative intent and public policy are interposed. Assume that, in a particular case, it becomes essential, or at least beneficial and convenient, to a full exercise of expressly granted corporate powers, that the corporation enter into partnership relations with an individual or an association. What, if any, implication arises as to legislative intent?⁸ On the one hand, it is

⁵*Pittsburgh Rys. v. Pittsburgh*, (1910) 226 Pa. St. 498, 75 Atl. 681.

⁶*Mallory v. Hananer Oil Works*, (1888) 86 Tenn. 598, 8 S. W. 396; *People v. N. River Sugar Ref. Co.* (1890) 121 N. Y. 582, 24 N. E. 834. *Franz v. Wm. Barr Dry Goods Co.*, (1908) 132 Mo. App. 8, 111 S. W. 636; *Boyd v. Am. Carbon-Black Co.*, (1897) 182 Pa. St. 206, 37 Atl. 937.

⁷*Koehler & Co. v. Reinheimer*, (1898) 26 App. Div. 1, 49 N. Y. S. 755.

⁸In the construction of charters and of articles and other instruments of incorporation, the primary object is to find and to make effective the intention of the legislature and of the incorporators, insofar as is possible. See *Union Nat'l Bank v. Matthews*, (1878) 98 U. S. 621, 25 L. Ed. 188; *Boston & L. Ry. Corp. v. Salem & L. Ry.*, (1854) 2 Gray (Mass.) 1; *White v. Syracuse & U. R. R.*, (1853) 14 Barb. (N.Y.) 559; *Whetstone v. Ottawa Univ.*, (1874) 13 Kan. 339.

claimed that the legislatures have very generally expressly provided that a corporation shall be managed, as to certain powers, by its stockholders, and, as to certain other powers, by a board of directors who shall be chosen by the stockholders, and still other powers shall be exercised by other officers of the corporation, and that, by the generally accepted rules of partnership law, there is a mutual agency whereby each partner may bind and may be bound by every other partner, aside from contractual restriction known by third parties. By reason of this situation, it is claimed that the corporation may be bound by persons or associations not contemplated by law, and that this situation precludes any presumption of legislative intent to imply an authority contravening such positive management provisions.⁹

This theory has been adhered to by the great majority of the courts, but its logical application may well be questioned. The inherent nature of the corporation necessarily implies that all its acts must be performed by agents. It has neither physique nor mentality by means of which it may act in person. Certain agency functions are lodged in the stockholders as a group, others in directors. Officers of the corporation may bind it in various matters. The same may be true as to mere agents.¹⁰ If a corporation may appoint a stranger as its agent to bind it in contract or in tort, or even to act as general manager, why is it beyond comprehension that it may appoint the other partners, in a partnership of which it is a member, to be such agents?

Is it true that there are certain elements of an agency through partnership that differ from those of an ordinary agency? As stated in one case:¹¹

"If a corporation be a member of a partnership, it may be bound by any other member of the association, and in doing so he would act, not as an officer or agent of the corporation, and by virtue of authority received from it, but as a principal in an association in which all are equal, and each capable of binding the society by his acts. The whole policy of the law creating and regulating corporations looks to the exclusive management of the affairs of each corporation by the officers provided for or

⁹*Fechteler v. Palm Bros. & Co.*, (C.C.A. 6th Cir. 1904) 133 Fed. 462; *Salem, etc., Ass'n v. McMahon*, (1915) 78 Or. 477, 153 Pac. 788; *Dong You v. Wing Hing Co.*, (1915) 22 Hawaii 660; *Gunn v. Central Ry.*, (1885) 74 Ga. 509.

¹⁰*Mallory v. Hananer Oil Works*, (1888) 86 Tenn. 598, 8 S. W. 396.

¹¹*Mallory v. Hananer Oil Works*, (1888) 86 Tenn. 598, 8 S. W. 396. See also, *Whittenton Mills v. Upton*, (1858) 10 Gray (Mass.) 582, 71 Am. Dec. 681.

authorized by its charter. This management must be separate and exclusive, and any arrangement by which the control of the affairs of the corporation should be taken from its stockholders and the authorized officers and agents of the corporation would be hostile to the policy of our general incorporation acts."

A fallacy of this argument lies in the assumption of a false premise. A partner of a corporation would be an agent of the corporation by virtue of authority received from the corporation in the articles of copartnership. In any partnership, the authority of one member to bind the other members is an agency granted by each one to each other one. The mere contract of partnership, without restriction, in itself gives this authority. Moreover, the management of the corporation, as is shown elsewhere herein,¹² need not be separate and exclusive, and there may be, in some instances, an arrangement by which the control of the corporation may be taken from such stockholders and authorized officers and agents of the corporation as are contemplated by the court in the above case.

It is contended that such elements of partnership agency as may differ from ordinary agency are logically immaterial to the subject under discussion. It may be argued that an ordinary agency is revocable at any time. But a partnership may be dissolved at any time, and in the case of a partnership at will the non-applicability of the reason for lack of the power under discussion can hardly be denied.¹³ The same is true in a limited partnership, where the corporation might be the sole general partner. It may be further argued that an ordinary agent may be directed and controlled or discharged by the principal, and that real control is in the firm. To a certain extent this is true as to agency between partners.¹⁴ It is not universally true in non-partnership agency, as some forms of agency may be irrevocable.¹⁵

There are some outstanding instances where the management and control of the corporate business have been, or may be,

¹²See notes 16 and 17.

¹³Allen v. Woonsocket Co., (1876) 11 R. I. 288.

¹⁴A partner's agency may be limited by agreement as between the partners, and as to third parties who have knowledge of the agreement. See, Shackleford v. Williams, (1913) 182 Ala. 87, 62 So. 54; Thomas v. Hardsocg, (1908) 137 Iowa 597, 115 N. W. 210; Feigenspan v. McDonnald, (1909) 201 Mass. 341, 87 N. E. 624; Uniform Partnership Act, sec. 9 (4).

¹⁵Hunt v. Rousmanier's Admrs., (1823) 8 Wheat. (U.S.) 174, 5 L. Ed. 589.

surrendered by the corporation. At this point it may be well to consider that there is a distinct difference between management of the corporation itself, and management of its business. Internal organization might readily be restricted to members. Even this internal organization, however, under certain conditions, may be surrendered. There are several outstanding instances where this has been done, either without challenge or where the power has been upheld by the courts; in some instances with legislative sanction, at other times without statutory authority.¹⁶

The instances cited in the footnote of such a practice of corporations without an enabling statute and without judicial sanction do not, of course, establish their own validity, but they are at least significant signs of the belief in their effectiveness and of an economic and business need therefor. The statutes authorizing such a practice at least negative any public policy which makes necessary an exclusive internal management of the corporation or of its business, at all times and under all circumstances and conditions. Moreover, there is a negative power of control and management, expressed in restrictive clauses in mortgages and other security devices, which is almost uniformly recognized by the courts and which is even more indicative of public policy.

Instances may also be given where corporations, as a device for securing creditors, have surrendered management of the whole business to these creditors, or have surrendered certain powers of management of their affairs.¹⁷

¹⁶A striking instance of such surrender of a management power, without challenge or legislative authority, is shown in the financial structure of The United States Shipbuilding Company, (See Moody, *The Truth About Trusts* 359 et seq.) where a certain large bond issue authorized a voting power in those bonds, equal to the same amount of stock. This practice, with variations, is shown in other bonds. Two issues of the Erie Railroad Company (First Consolidated Prior Lien Gold 4s, dated Dec. 10, 1895, and the First Consolidated Gen. Lien Gold 4s of the same date) provided that each one thousand dollars of these bonds should be entitled to ten votes at stockholders' meetings. The 5% income bond issue of the Chicago, Terra Haute & S. E. Ry. Co. is another instance of voting bonds.

In some instances voting by creditors has been recognized by statute. Ohio has had a statute (Page's Code of 1921, sec. 9079 et seq.) authorizing, in certain railroad re-organizations, the voting by creditors with stockholders. The statutes of Iowa, (Code of 1927 Sec. 7930) and of New Jersey, (Comp. Stat. of 1916, sec. 5, p. 4241) provide for voting by bondholders, under certain conditions, in railroad corporations. Delaware, (Rev. Code of 1915, sec. 29, p. 930) and Virginia (Gen. Laws of 1923, sec. 3808) extend this power, under certain limitations, to bondholders, in any corporation.

¹⁷The 4% Refunding 100 year Gold Bonds of the Metropolitan

A legislative act is commonly accepted as a declaration of public policy.¹⁸ Surely there is no public policy that there must be, under all circumstances and conditions, a complete retention and control by the corporation of exclusive powers of management of its business, even to the denial of a right of appointment (by partnership relation or otherwise) of agents with powers to incur certain liabilities for the corporation, and so to carry out the purpose of the acts of incorporation. There is, on the other hand, a presumption that the legislature intends its grant of corporate powers to be effective and that certain unenumerated powers are to be implied, if they are necessary or convenient to the accomplishment of expressly granted powers, and do not contravene public policy or positive law.

There is a minor list of authorities, more logical than the majority, that hold, in accord with this latter theory, that such power may be impliedly granted.¹⁹

In one case in particular, where a bank was compelled to take over a pledged stock of goods in the collection of a debt due to the bank, it was held that there was a power in the bank to enter into a partnership with the former owner, to operate the business for the purpose of realizing on the security, at least to the extent of the property put into the business by the bank.²⁰

This brings us to a consideration of the situation in those jurisdictions where the corporation is held to be incapable of be-

Street Railway Company (of New York) were made subject to a provision that, upon certain defaults on the part of the company, a trustee could enter in and operate the railway and the premises. The West India Sugar Finance Corporation, a Connecticut corporation, has had a peculiar system of securing control, either in the management of debtor corporations, or of the business of such other corporations. The principal business of this corporation was the financing of sugar companies in the West Indies. It secured a measure of control over these debtor corporations, not through stock ownership, but sometimes by taking complete management of the property of these other corporations, and in other instances it placed one or more representatives on the board of directors. It also had contracts with the other corporations, providing that capital expenditures and the payment of dividends should rest with the finance corporation.

Sec. 30, p. 955, Maine, R. S. expressly authorized trustees for bondholders in railroad corporations, upon default in payments on bonds, and upon an affirmative vote of the bondholders, to take over the railroad, with all the powers and obligations of the directors and of the corporation.

¹⁸In *re* Lampson's Will, (1898) 33 App. Div. 49, 53 N. Y. S. 531.

¹⁹*Butler v. American Toy Co.*, (1878) 46 Conn. 136; and see, *Catskill Bank v. Gray*, (1851) 14 Barb. (N.Y.) 479.

²⁰*Snow Hill Bkg. Co. v. D. J. Odom Drug Co.*, (1924) 188 N. C. 672, 125 S. E. 394. And see 9 *Minnesota Law Review* 381.

coming a partner. Is a corporation, by reason of this theory, in attempting partnership relations, insulated from any rights or liabilities growing out of such an attempt to establish such forbidden relation? As in other ultra vires contracts, it is not necessarily true that, because the attempted contract does not establish the attempted relation, no rights or liabilities attach to the corporation. The remedy pursued and the question whether the act contemplated is executory, executed or partly executory and partly executed must be taken into consideration. The element of estoppel also becomes material. There is a wide difference between liability *as a partner* and liability *as if a partner*.

Even in a jurisdiction where partnership relations are held to be ultra vires, it is hardly conceivable, in a business venture between a corporation and others, where there would be a partnership were the relation not ultra vires of the corporation, and where the business was fully completed and the proceeds divided, that a court would generally give any affirmative relief to either party in an action to secure all the benefits of the transaction, merely on the ultra vires aspect of the case²¹ even though in such a jurisdiction a court of equity, in an action for specific performance, might deny relief where the contract was wholly executory. In case the contract was wholly executory on one side and wholly executed on the other, the courts are divided on the question of allowing the one receiving the benefits to repudiate the contract, with perhaps the better reasoned line of authorities refusing to permit this practice.

In view of the vague line of demarcation between partnerships and joint adventures, it is a peculiar but significant fact that a corporation, although not considered, by the weight of authority, to have capacity to enter into a partnership, without statutory authority therefor, may, nevertheless, enter into joint adventures with others for any transactions which are not, in themselves, ultra vires of the corporation, even though partnership liability is thereby incurred by the corporation.²² And the mere joint

²¹Boyd v. Amer. Carbon-Black Co., (1897) 182 Pa. St. 206, 37 Atl. 937.

²²Salem-Fairfield Tel. Ass'n v. McMahan, (1916) 78 Or. 477, 153 Pac. 788; Clinchfield Fuel Co. v. Henderson Iron Works Co., (C.C.A. 5th Cir. 1918) 254 Fed. 411; Quitman Oil Co. v. McRee, (1916) 18 Ga. 128, 88 S. E. 921; Mestier v. A. Chevalier Pav. Co., (1901) 118 La. 562, 32 So. 520.

interest growing out of an attempted partnership has been held sufficient to bind corporations to liability therefor.²³ It would appear that a somewhat arbitrary rule, denying partnership capacity to a corporation, has been quite generally recognized by the courts, as a matter of *stare decisis*, but that they, realizing its defects in many instances, have seized upon various devices to evade its effective operation whenever occasion has urgently demanded. The recognition by some courts of the power of a corporation to enter into joint adventures, while at the same time recognizing the rule that precludes the partnership relation, is such a subterfuge.

A joint adventure has been termed "an association of two or more persons to carry out a single business enterprise for profit."²⁴ Certain jurisdictions point out minor distinctions between a partnership and a joint adventure, but the common and principal one seems to be merely that the joint adventure is limited to one transaction rather than to a series of transactions. However, a partnership may be confined to a single transaction.²⁵

In view of this situation, it is obvious that, in most jurisdictions, a distinction relating to the problem under discussion herein, which is based upon the difference between a partnership and a joint adventure is largely one of terminology, and obviously a mere subterfuge. Even where a difference between a partnership and a joint adventure is recognized at all, it has been held that the relations are very similar,²⁶ and that they are governed by practically the same rules of law.²⁷

²³*French v. Donohue*, (1882) 29 Minn. 111, 12 N. W. 354; *N. Y. & S. Canal Co. v. Fulton Bank*, (1831) 7 Wend. (N.Y.) 412; *Wilson v. Carter Oil Co.*, (1899) 46 W. Va. 469, 33 S. E. 249.

²⁴*Rowley*, *Modern Law of Partnership*, sec. 975. See, *Goss v. Lanin*, (1915) 170 Iowa 61, 152 N. W. 43; *Felbel v. Kahn*, (1898) 29 App. Div. 270, 51 N. Y. S. 435. Compare, *Pollock*, *Partnership*, 11th ed., pp. 6, 7.

²⁵*Spencer v. Jones*, (1899) 92 Tex. 516, 50 S. W. 118; *Cochran v. Anderson Co. Nat'l Bank*, (1884) 83 Ky. 36.

²⁶*Slater v. Clark & Co.*, (1896) 68 Ill. App. 433; *Irvine v. Campbell*, (1913) 121 Minn. 192, 141 N. W. 108; *Doane v. Adams & Co.*, (1860) 15 La. Ann. 350.

²⁷*Hulett v. Fairbanks*, (1883) 40 Ohio St. 233; *Goss v. Lanin*, (1915) 170 Iowa 61, 152 N. W. 43. *Ross v. Willett*, (1894) 76 Hun 211, 27 N. Y. S. 785; *Church v. Odell*, (1907) 100 Minn. 98, 110 N. W. 346; *Marston v. Gould*, (1877) 69 N. Y. 220.

SUMMARY AND CONCLUSION

A perusal of the cases seems to indicate that a majority have held that, without express statutory sanction, a corporation has no authority to become a partner, that there is no implied authority therefor which arises from necessity or convenience in carrying out the express powers granted to the corporation, and that a main reason therefor is to be found in the usual provisions of corporation statutes implying an internal control of each corporation, which would be surrendered by entering into a partnership where other partners could control, or at least bind, the corporation.

Certain statutes have been cited, however, which seem to negate any universal public policy that the corporation and its business must, under all circumstances, be internally managed. It has also been shown that, in many instances, outside control has been permitted, without express statutory authority, but without objection, contest, or judicial determination. Even the cases denying the power of a corporation to become a partner without express authority do not generally deny its power and right to become a joint adventurer, in a very similar association, with partnership liability and with practically all the basic reasons against such a relationship as may be found in a partnership. Furthermore, many of these cases concede that, even though a corporation cannot become a partner, it may, in many instances, assume partnership liability as if a partner, by estoppel or otherwise.

The cases denying partnership capacity are founded upon a narrow, illogical and somewhat obsolete philosophy and viewpoint. The theory became established when there was a popular and legislative antipathy toward the corporation, indicating a legislative intent to preclude any large measure of implied powers. At that period, owing to the comparatively small number and size of corporations, it is possible that there was an uncertainty as to the advisability of the corporate form of business association, which, in itself, created a public policy of a very real importance against any extended implication of corporate powers at that time.

At the present time this situation has changed. The corporation has justified itself as a means of business association. It has become greatly extended, both as to size and in numbers. Its implied powers have increased. No longer does its very newness

imply a public policy or a legislative intent to unduly restrict implied powers, provided these implied powers are not opposed to positive law, and are necessary or convenient in the furtherance of its express powers. A lack of public policy against such implied powers is indicated in the provisions of the Uniform Partnership Act.

The subterfuges employed by the courts to give the corporation many of the rights and to impose upon it many of the liabilities that it would have were the true partnership permissible indicate an antipathy on the part of the courts to the rule denying partnership capacity to a corporation. Moreover, the fact that a small minority of the cases have conceded the right of a corporation to enter into real partnership relations, with all of the rights and liabilities of any partners, even without express statutory authority therefor, shows an increasing policy, based upon business needs and a more rational method of approach by these courts, to adopt more direct and sensible rules for the determination of the problem under discussion.