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holding in Pennsylvania on this point, it is submitted that our courts will apply the general rule as to prior creditors in accordance with the view taken by the majority of states.

Edgar K. Markley.

IS PA. SWINGING TO THE FEDERAL RULE ON CORPORATE ULTRA VIRES CONTRACTS?

"Contracts ultra vires of the corporation making them are not merely voidable but wholly void and of no effect and no performance by either party can give the unlawful contract any validity." This startling statement was recently made by the Pennsylvania Superior Court, in a decision involving Pennsylvania law, and dealing with a Pennsylvania corporation.¹

Bedell, the plaintiff, was an employee of the Oliver H. Bair Co. funeral directors, the defendants. While so employed, the plaintiff executed a "Benefit Bond" wherein it was agreed between the plaintiff and defendant that in consideration of the payment of forty-six cents (\$.46) quarterly during the term of the plaintiff's life, the defendant Co. would "care for and inter the remains" of the plaintiff at a total cost of \$75. Failure to pay for three months worked a forfeiture of the agreement. Plaintiff in pursuance thereof paid the quarterly sums for twenty-eight years, in the aggregate amount of \$51.74. Being advised that the contract was illegal, the plaintiff demanded from the defendant the amount paid in and upon defendant's refusal to refund the amount, sued in assumpsit. The Superior Court, through Judge Cunningham, affirmed the opinion of Judge Finletter in the court below finding that the contract was one of insurance, was clearly ultra vires of the defendant corporation, was *therefore* utterly void and of no effect, and no action could be based upon it! However, as suit was brought in assumpsit the court allowed a quasi-contractual recovery by the plaintiff.

¹Bedell v. Oliver H. Bair Co. Inc., 158 Atl. 651.

Not a single Pennsylvania case appears in that part of the opinion dealing with *ultra vires*, in support of the position taken by the court, in spite of the fact that in an earlier Supreme Court opinion dealing with the defense of *ultra vires*² it was pointed out that "the cases are legion" to the effect that *ultra vires* is no defense in such an action on the contract. Moreover, in distinct contradiction to such overwhelming authority in Pennsylvania the court quotes at length from Justice Gray's opinion in the *Pullman Palace Car Co.* case³ and the discussion appendant thereto in Professor Keener's work on *Quasi Contracts*.⁴

As early as 1847 in Pennsylvania the principle underlying the modern majority rule on *ultra vires* as a defense to corporate contracts—that one who has received benefits under an illegal contract should not be allowed to avoid the contractual burdens—was asserted by our Supreme Court.⁵ The first decisive proclamation of this view however, was made in 1876 in the case of the *Oil Creek and Allegheny Railroad Co. v. Pa. Transportation Co.*⁶ In that case, the defendant railroad in its first agreement with the plaintiff transportation company stipulated that it would pay the plaintiff ten cents a barrel rebate on all oil, the freight charge for which was forty-five cents or more per barrel; a proportionately lower rebate on all oil shipped the freight charge for which was less than forty-five cents per barrel; but no rebate on any oil for the carriage of which the freight charge was less than twenty cents per barrel. Sometime later the defendant railroad suggested a modification of the contract, to which the plaintiff assented, to the effect that instead of the varying rebates, a flat rebate of five cents per barrel would be paid, regardless of the freight rate. At the time of the modification, freight rates were falling and the defendants soon found

²286 Pa. 405, at 412, 133 Atl. 551, quoting from 254 Pa. 422, 429, 98 Atl. 1052.

³*Central Transportation Co. v. Pullman Palace Car Co.*, 139 U. S. 24, 59, 11 Supreme Court Reporter 478, 35 Lawyer's Edition 55.

⁴Page 272, note 1.

⁵Gibson, C. J. in *Lestapies v. Ingraham*, 5 Pa. at page 81.

⁶83 Pa. 160.

that by the modification it had made a bad bargain. Having failed to pay the rebates agreed upon, the plaintiff sued the defendant in an action of debt, defendant setting up that the contract was *ultra vires*, illegal and void, and hence no recovery could be had upon it. Paxson, J., in deciding for the plaintiff said: "We do not think the defendants are in a position to defend upon the ground of the illegality of the contract. There were mutual covenants and mutual advantages. The defendants had enjoyed the advantages, such as they were. To the extent of the demand in this suit, the contract was executed, and to say now that it is *ultra vires* comes with an exceedingly bad grace from the defendants. It may be that having shown performance on their part they would have a right to rescind the contract as to future transactions upon the ground of illegality. But there is no rule of law which permits them to retain both the benefits and the price." The forceful language of this opinion was expressly approved and the rule of the case followed in the later case of *Wright v. Pipe Line Co.*⁷

In the case of *Railroad Co. v. Railroad Co.*⁸ a situation analogous to the one under discussion, so far as the fate of the case in the lower court was concerned, presented itself. But it was disposed of by the appellate court in different fashion from the present controversy. In that case the lower court held that a lease made between the parties, on which suit was brought, being *ultra vires*, was null and void. The Supreme Court reversing said, "In the present case the cry of *ultra vires* is made by a party to the contract—to the executed agreement from which it has already derived some benefit. If it is *ultra vires* now, it was *ultra vires* then, when the contract was solemnly entered into by the appellee, and equity will turn a deaf ear for relief from a compact intelligently and deliberately made when prayed for by a party to it, whose conscience has become quickened only when hopes are disappointed and

⁷101 Pa. 204, 47 Am. Reports 701.

⁸196 Pa. 452, 46 Atl. 431.

expectations not realized." Then follows a quotation from the leading cases discussed above.⁹

The case of *Boyd v. American Carbon Black Co.*¹⁰ is an interesting one on the subject of ultra vires contracts. Boyd entered into a partnership agreement with the Carbon Black Co., which was at the time of the agreement, only an association of individuals, whereby he furnished gas for the company's use, acquiring therefor a one-fifth interest. Later the Co. was incorporated, Boyd buying stock therein, later becoming a director. The corporation succeeded to all the partnership rights under the agreements. The corporation made another contract with Boyd, stipulating that it would, jointly with Boyd, erect another small factory, use the excess gas from Boyd's wells to make carbon black and divide the profits so made. In violation of the agreement the company stopped operations at the new factory, and agreed with the Columbian Co. to sell to it its products, the profits to be divided equally, the defendant company to shut down for one year, etc. Plaintiff brought a bill in equity to have the agreement declared void, for an accounting, dissolution of the partnership under the second agreement, and other relief. The defense interposed was that a corporation could not enter into a partnership agreement; hence, being ultra vires, the contract was null and void and no action could be brought upon it. The court said in part: "The principal reason given by the learned judge of the court below for sustaining the demurrer is that the contract of partnership by the corporation was ultra vires; that no corporation has authority to share its corporate management with natural persons in a partnership****. Assume that the partnership has not now and never had a legal existence;**** while it had no *legal existence* it had one in fact; and the other partner fully performed; the corporation had the full benefit of the contract up to the time that it concluded that it was more profitable to violate its agreements. 'It

⁹Wright v. Pipe Line Co., 101 Pa. 204; Oil Creek and Allegheny River Railroad Co. v. Penna. Transportation Co., 83 Pa. 160.

¹⁰182 Pa. 206, 37 Atl. 937.

may be prima facie ultra vires for an incorporated company to enter into a partnership with other persons' but all the authorities hold that, notwithstanding the prima facies, if it be shown that the other partner had fully performed his obligations under the contract, this plea will not avail. 'A corporation may not avail itself of the defense of ultra vires when the contract has been in good faith performed by the other party, and it has had the full benefit of the performance and of the contract'."

*Trust Co. v. Library Hall Co.*¹¹ involved a mortgage transaction which was ultra vires. The defendant company had been restricted by the legislature in the total amount of mortgage indebtedness it could contract. It executed a mortgage to the plaintiff trustees, who issued bonds on the security thereof to various persons in small denominations. On foreclosure of the mortgage, the defense was that the contract was ultra vires, null and void. The court said: "But assuming that by legislative language somewhat obscure the authority to borrow \$150,000 additional was doubtful, the corporation, this mortgagor, will not be heard to raise the question of ultra vires. It assumed to have authority to mortgage, received the money, and applied it to corporate purposes. "The law never sustains a defense of this nature out of regard for the defendant'."

From these decisions, it is apparent that so far as Pennsylvania is concerned the modern majority rule as to the effect of ultra vires on a corporate contract, and not the Federal rule as asserted in the *Pullman Co.* case,¹² is the law of Pennsylvania. More than a score more cases to the same effect could be cited for the same proposition.¹³

It is true that the case under discussion does vary

¹¹189 Pa. 263, 42 Atl. 129.

¹²See note 3.

¹³A few of the more prominent cases are *Wrightsville Hardware Co. v. McElroy*, 254 Pa. 422 at 429, 98 Atl. 1052; *Ramble v. Pa. Coal Co.*, 47 Pa. Super. Ct. 28, 39; *Lemon v. E. Palestine Rubber Co.* 260 Pa. 28, 33, 103 Atl. 510; *Cameron v. Christy*, 286 Pa. 405, 411, 133 Atl. 551; *Presbyterian Board for the Relief of Disabled Ministers v. Gilbee*, 212 Pa. 310, 61 Atl. 925; also 14a C. J. p. 320, note 88; also *Fletcher on Corporations*, No. 1541 to 1547.

materially in its facts from some of the cases discussed, for here the contract is being rescinded, the action being for money had and received, while in the previous cases the contract was being affirmed and an action for its breach or similar redress pursued. Nor is there any fault to find with the conclusion reached by the court, for admittedly it was just and equitable. But, it is submitted, the court erred in accepting as the basis for its conclusion, the federal view that the contract being ultra vires was null and void. More consonant with the prior Pennsylvania law on the subject would have been the legal theory—ratio decidendi—that the contract so far as executed, was valid; that the corporation by its act was estopped to deny its validity as being ultra vires; but as the contract was made under a mutual mistake it could be rescinded by the performing party and an action for money had and received, in quasi contract, brought, wherein any performance by the corporation could be set up in defense.

Loose statements such as this, while seemingly trifling, have furnished no end of trouble in the law, have led to absurd conclusions and palpable injustices, as evidenced by the contortion of a famous maxim in *Bilbie v. Lumley*¹⁴ and should be carefully guarded against by our courts.

Robert E. Knupp

¹⁴2 East 469, per Ellenborough, L.C.J.—Ignorantia legis neminem excusat.