

## NOTES

**BUSINESS ORGANIZATION—INTERRELATIONSHIP OF CORPORATIONS AND NON-PROFIT ASSOCIATIONS—RIGHTS AND LIABILITIES OF MEMBERS.**—A fundamental purpose for the creation of a corporation is to subserve the public welfare and convenience by bestowing the character of individuality upon a combination of capital and individuals, for the accomplishment of such things as may not be so well or so readily achieved by a single person, and that may not be ended by the death or withdrawal of a part of the members. Being created by authority of statute, and endowed with certain rights and obligations, it is recognized as an artificial person, possessed of the right to sue and be sued, and to hold title to property in the corporate name. The interests of its members are represented by shares transferable without effecting a dissolution or modifying the status of the corporation.

On the other hand, in the absence of an enabling statute defining the rights and liabilities of members, societies, associations, partnerships, and other bodies combined under their own rule for their private benefit, and without any express sanction of law, are not, in the collective capacity and name, recognized at common law as having any legal existence distinct from their members; hence they have no right to sue or be sued in the company name. Such unincorporated associations, so far as rights and liabilities are concerned, are *treated* as partnerships, or joint enterprises, and to enforce rights for or against them, the names of all members liable must be set forth either as plaintiffs or defendants.<sup>1</sup>

The position such unincorporated associations occupy under the law is a question upon which the courts are not generally agreed. It is acknowledged that they are "sui generis," but courts have had difficulty in agreeing upon the legal principles to apply to them. Many cases hold that in some of their relations they are to be regarded as co-partnerships and governed by general laws applicable to that relationship, and that in other respects the law of corporations applies to their affairs. The distinction in this respect is made (1) as to cases involving rights between the association and third persons dealing with it, and (2) as to cases involving controversies between members respect-

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<sup>1</sup> *Hays v. Lanier*, 3 Blackf. (Ind.) 322; *Atkins v. W. A. Fletcher Co.*, 65 N.J.Eq. 658, 55 Atl. 1074 (Ch. 1904); *Pickett v. Walsh*, 78 N.E. 753 (1906).

ing property owned by the association. Such associations are properly divided into two classes, *viz*; those organized for the purpose of conducting some business enterprise, and those whose purpose is solely the promotion of the interests and welfare of their members, unaccompanied by any business function. As to this class it would seem the law of principal and agent should apply.<sup>2</sup> In *Burton v. Grand Rapids School Furniture Co.*,<sup>3</sup> the court states:

“ . . . An unincorporated association is no person and has not the power to sue or to be sued. When such an association has been organized and is conducted for profit, it will be treated as a partnership, and its members will be held liable as partners. But in the case of religious or eleemosynary associations, the members and managing committee who incur the liability, assent to it or subsequently ratify it, become personally liable. . . .” This clearly is an application of the general law of principal and agent, recognized again in *McGreary v. Chandler*.<sup>4</sup>

Having no separate entity, the property of such non-profit unincorporated associations is deemed to be the joint ownership of their members, who have consequently the right to control, manage and dispose of it at their pleasure, subject to the provisions and stipulations of the contract under which it is held, as contained in the constitution, by-laws or other rules adopted by the society.<sup>5</sup> The right to adopt a constitution, rules and by-laws is within the scope of the lawful purposes of the organization, and binds the members thereby.<sup>6</sup> They may provide and impose penalties for failure of members to comply with the regulations, enforceable in the courts.<sup>7</sup>

1. Where the charter of a local union or association is revoked by the general union, courts will not interfere to restore it, where no property rights are involved, until the remedies provided within the

<sup>2</sup> *Ehrmountraut v. Robinson*, 52 Minn. 333, 54 N.W. 188 (1893).

<sup>3</sup> 10 Tex. Civ. App. 270, 31 S.W. 91 (1895).

<sup>4</sup> 58 Me. 537 (1870).

<sup>5</sup> *Torrey v. Baker*, 1 Allen (Mass.) 120 (1861); *Duke v. Fuller*, 9 N.H. 536, 32, Am. Dec. 392 (1838).

<sup>6</sup> *Mayer v. Journeymen Stone-Cutters' Association*, 47 N.J.Eq. 519, 20 Atl. 492 (Ch. 1890); *Brown v. Stoerkel*, 74 Mich. 269, 41 N.W. 921, 3 L.R.A. 430 (1889).

<sup>7</sup> *Master Stevedores Association v. Walsh*, 2 Daly (N.Y.) 1 (1867).

association have been exhausted. The rights of membership evidenced by a charter granted by a general to a local union are not property rights nor does membership therein confer such property rights as are necessary to give the courts jurisdiction.<sup>8</sup> Decisions of the general union in admitting, suspending or expelling members are of a quasi-judicial character, and courts will not interfere except to ascertain whether the proceedings are in accordance with the rules and laws of the association, in good faith, or in violation of the laws of the land.<sup>9</sup>

As a general rule, subject to local exceptions and to exceptions founded on special considerations, one corporation cannot become a shareholder in another unless such power is given by its charter or governing statute.<sup>10</sup> The leading principle which restrains a corporation from so investing is that it is unlawful to employ funds in a way not permitted, to deflect them from the purposes designated by its own charter. Consequently, the principle does not apply where two corporations are created for similar purposes.<sup>11</sup> A few decisions are met with where the view is taken that a corporation may invest in stock of other corporations provided it be done *bona fide* and with no unlawful purpose, and there be nothing in its charter or in the nature of its business which forbids it.<sup>12</sup> Many statutes and charters recognize or confer this power.<sup>13</sup> Where the view obtains that such investment is permissible, the ordinary liabilities of a shareholder attach to the corporation which so acts.<sup>14</sup>

It is not unusual for such non-profit associations to incorporate and to organize subsidiary unincorporated associations under charters granted by the corporation. It is clear that the relation between the corporation and its chapters, and the members thereof, is one exclu-

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<sup>8</sup> O'Brien v. Musical Mutual Protective Union, 64 N.J.Eq. 525, 54 Atl. 150 (Ch. 1903).

<sup>9</sup> Froelich v. Musicians Mutual Benefit Association, 93 Mo. App. 383 (1902); Beesley v. Chicago Association, 44 Ill. App. 278 (1892).

<sup>10</sup> 31 N.J.Eq. 470, 8 Atl. 130 (Ch. 1879). See N. J. P. L. 1932, p. 272.

<sup>11</sup> Electric Securities Co. v. Louisiana Electric Light Co., 68 Fed. 673 (1895); *In re Asiatic Banking Corporation*, L. R. 4 Ch. 252.

<sup>12</sup> Booth v. Robinson, 55 Md. 419 (1880); Hill v. Nesbit, 100 Ind. 341; Evans v. Bailey, 66 Cal. 112, 4 Pac. 1089 (1884).

<sup>13</sup> See N. J. P. L. 1888, c. 269, p. 385.

<sup>14</sup> McKim v. Glenn, 66 Md. 477, 8 Atl. 130 (1887).

sively of contract. The constitution, rules and by-laws constitute the contract of membership, and ordinarily no rights of membership can arise unless the provisions thereof are assented to.<sup>15</sup> The rights and liabilities of the members are determined by the corporate charter, or the statute under which the corporation was organized. They are liable, if at all, according to the domicile of the corporation.<sup>16</sup> The laws are regarded as rules of property, and if not against public policy, are enforced.<sup>17</sup>

There is no inconsistency, *ipso facto*, in the incorporation of a subsidiary non-profit association, where the purposes remain the same. It would seem that unless the intention is clear to withdraw from the parent corporation, there being no question of shareholding, and the purposes of both corporations being similar, the members of the new corporation retain their rights and liabilities under their original charter, unless so inconsistent with the character of the new corporation as plainly to require withdrawal.<sup>18</sup> If one corporation may invest in the stock of another where no unlawful purpose is intended and the nature and character of the business of both are similar, then, *a fortiori*, an incorporated non-profit association may be a member of another corporation organized for the same purpose. And if such incorporation is, by the terms of the original charter, a breach thereof, the problem presents itself as to the rights and liabilities existing between the members of the quondam association and the parent corporation consequent upon such breach.

It is the general principle that until the corporation is legally organized, the coadventurers will be liable as partners for all debts contracted on behalf of the aggregate body, with their consent express

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<sup>15</sup> *Konta v. St. Louis Stock Exchange*, 189 Mo. 26, 87 S. W. 969 (1905).

<sup>16</sup> *Halsey v. McLean*, 12 Allen 438, 90 Am. Dec. 157 (1866); *Glenn v. Liggett*, 135 U. S. 533, 34 L. ed. 262 (1889).

<sup>17</sup> *Chase v. Curtis*, 113 U. S. 452, 28 Fed. 1038 (1884).

<sup>18</sup> *Strong v. Walnut Growers' Assn.*, 137 Cal. 607, 70 Pac. 734 (1902), *held*, "Persons who have become members of a voluntary association, and have not formally withdrawn therefrom, are entitled to the rights of members although they have formed a corporation with the intention of substituting it for the association, it not appearing that they intended to abandon their rights as members of the association."

or implied.<sup>19</sup> If an unincorporated association contracts liabilities and then incorporates, the members of the association liable before incorporation *remain* primarily liable jointly and severally for said debts. The responsibility of the corporation does not become substituted, without the creditor's consent, so as to exempt the members from individual liability.<sup>20</sup> But the corporation becomes also primarily liable for the existing indebtedness of the company. Creditors thus retain their security, *viz.*, the individual liability of members now incorporated.<sup>21</sup> Existing creditors of the association may discharge the latter from personal liability and substitute the credit of the corporation as by continuing the previous course of dealing. Certainly, if by the terms of the original charter, an association, by incorporating, has forfeited that charter and the association assets to the parent corporation, incorporation will not relieve it of that obligation, nor its members, where the rights of third parties are not involved. And the same result should follow where a forfeiture occurs after incorporation, where the incorporation itself does not constitute a withdrawal from the original charter, and the rights and liabilities of association membership are intended to be, and were retained.<sup>22</sup>

The problem is very much the same in cases involving a foreign parent corporation having subsidiary chapters locally situated. It is acknowledged that the charter, if valid in the state of incorporation, is valid and binds the members in the local state unless repugnant to its fundamental law or public policy. It operates among the members as the law of the corporation, and hence, strictly as between the association members and the corporation, that contract of membership governs their relations and creates the rights and liabilities arising therefrom, according to the laws of the state of incorporation.<sup>23</sup> Every member is presumed conclusively to know the terms and provisions of the association charter, and of the constitution and by-laws of the corporation. If by those provisions an association has forfeited its charter

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<sup>19</sup> *McDowell v. Joice*, 149 Ill. 124, 36 N. E. 1012 (1893); *Fuller v. Rowe*, 57 N. Y. 23 (1874); *Guckert v. Hacke*, 159 Pa. St. 303, 28 Atl. 249 (1893).

<sup>20</sup> *Broyles v. McCoy*, 5 Sneed (Tenn.) 602 (1858).

<sup>21</sup> *Haslett v. Wotherspoon*, 1 Strobb. Eq. (S. C.) 209 (1847).

<sup>22</sup> *Fidelity and Deposit Co. of Maryland v. Brotherhood of Painters, Decorators and Paperhangers of America, et al.*, 120 N.J. Eq. 346, 184 Atl. 832 (Ch. 1936).

<sup>23</sup> *Ex parte Van Riper*, 20 Wend. (N. Y.) 614 (1839).

and assets, it is no defense that the association has become a corporation under local statute, where such incorporation is not a surrender of the rights of association membership. *A fortiori*, where incorporation itself constitutes forfeiture.