

CHAPTER ONE

HISTORY

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Section 1.01 English Corporate Law

Although a form of corporation existed under Roman law, corporations as we know them today are a modern invention. The first English trading company, The Merchant Adventurers of England, began in 1359. 1 FLETCHER CYC CORP § 1 n 3 (Perm Ed 1999). The first English corporations to enjoy the modern concept of shareholder limited liability were first formed with passage of the English Limited Liability Act of 1855.

Incorporation in England originally was granted only as a royal favor or special parliamentary privilege. It was not until the nineteenth century, when general corporation laws were enacted, that it became a right open to all people.

At common law, the Crown long had the right to grant charters of incorporation. See, generally: Holdsworth, *English Corporation Law in the 16th and 17th Centuries*, 31 YALE L J 382 (1921). In the sixteenth and seventeenth centuries, the Crown granted these charters to trading companies for the development of foreign trade. Thus, the first large business corporations in England were the "quasi-governmental" foreign trading companies, chartered for the purpose of exploration, colonization, and trading overseas. Such companies included The East India Company, chartered in 1555; the African Company, chartered in 1619; The Bank of England, in chartered in 1674; and the South Sea Company, chartered in 1711. "The Governor and Company of Adventurers of England Trading into Hudson Bay," popularity known as the "Hudson Bay Company," was granted a royal charter by Charles II in 1670 and it still exists today. *The Governor and Company of*

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Adventurers of England Trading into Hudson's Bay v. Hudson Bay Fur Co., 33 F2d 801 (1928).

Trading companies were originally regulated companies, that is, companies in which each member conducted the business of trade within the rules of the company. For instance, in *The East India Company*, an investor subscribed only for a particular voyage and accounts of each voyage were kept separately. Each member was free to invest or not invest in any given venture. It was the regulatory structure of the company which was permanent and constant, not its ownership. W. HOLDSWORTH, VIII, *A HISTORY OF ENGLISH LAW* 206-219 (2d Ed 1937).

The English forerunners of the modern business company were not these large, regulated, chartered trading companies, but rather, the unincorporated joint stock companies which emerged towards the end of the seventeenth century. In a joint stock company, the company invested in ventures as a single entity with stock owned jointly by all of its members. Initially, these joint stock companies were formed only by special act of Parliament, or by grant of charter.

The first legislative enactment related to joint stock companies is popularly referred to as the "Bubble Act of 1720." It was enacted in response to wild stock speculation, culminating in a stock value crash in 1720, and accompanied by widespread perceptions of fraud. BANNER, *ANGLO-AMERICAN SECURITIES REGULATION*, 41-87 (1998); W. HOLDSWORTH, VIII, *A HISTORY OF ENGLISH LAW* 219-222 (2d Ed 1937).

The concept of limited liability initially appeared in the Bubble Companies Act, enacted in 1825. Under it, when granting charters, the Crown was empowered to provide that the members of a corporation were personally liable for corporate debts to such an extent as the Crown thought proper.

Parliament enacted the Chartered Companies Act in 1837 and the Joint Stock Companies Registration Act in 1844. In 1855, it enacted the Limited Liability Act, which formally introduced the concept of shareholder limited liability into English company law. The 1855 Act limited shareholder liability to the subscription price of the shares, often an amount greater than the initial subscribers actually paid for their shares.

The Companies Act of 1862 repealed and consolidated the then-

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existing Acts. It opened the right to incorporate to all persons under a general law and without a special act of Parliament. T.E. CAIN, CHARLESWORTH AND CAIN COMPANY LAW 8-9 (11th Ed 1977); H.W. BALLANTINE, BALLANTINE ON CORPORATIONS 35 (1946). This Act was influenced by the corporation laws developed in New York and other American states. In turn, these English laws were used as models by the various American states as they developed their own corporation statutes.

Section 1.02 United States and Washington Corporate Law

A. Early statutes.

English corporate law was carried over to the American Colonies. In the post-revolutionary period, state legislatures assumed the powers of the English Crown and corporate charters were granted through private bills, sometimes referred to as a "special acts." HAMILTON, CASES AND MATERIALS ON CORPORATIONS 118 (1976). It was a power sparingly used. At the start of the nineteenth century, there were only about two hundred corporations chartered in the United States. HENN ON CORPORATIONS 16 (1961).

Gradually, all states adopted statutes permitting individuals to incorporate under general laws, rather than by special act of their legislatures. The first general incorporation act for canal companies was enacted by North Carolina in 1795. Garrett, *Model Business Corporation Act*, 4 BAYLOR L REV 412 (1952). This was followed by the first general incorporation act for manufacturing companies, adopted by New York in 1811, which was followed by similar laws in Massachusetts, Michigan, and Connecticut in the 1830's. Brockelbank, *The Compensation of Promoters*, 13 OR L REV 195, 200 (1934).

Another form of organization which had popularity in the nineteenth century were common law trusts, commonly referred to as "Massachusetts Trusts."

Common law trusts attained popularity in Massachusetts, being there used for the purpose of evading restrictions on the right of corporations to deal in real estate. As gradually developed, they became known as "Massachusetts Trusts", becoming elaborate types of business organization largely resembling corporations whose advantages they sought to acquire, and whose disadvantages they sought to eliminate. Nevertheless courts were often inclined to impose unlimited partnership liability on certificate holders, or strict personal liability on trustees, as well as to occasionally make applicable to such trusts tax and other statutes dealing with corporations. (citations omitted) Horowitz, "*Disregarding the Entity of Corporations*," 14 WASH L REV 285, n 3 (1939).

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B. Constitutional prohibitions against incorporation by special act.

Until the early part of the nineteenth century, corporations could only be formed through a private bill, sometimes referred to as a "special act," which would need to be passed by both legislative houses and signed by the state's governor. This procedure was subject to favoritism and corruption.

An example of one of these "special acts," one incorporating the "Washington Woolen Manufacturing Company," can be found in 1864-5 Washington State Session Laws 144.

In the Nineteenth Century, Americans looked unfavorably at the favoritism and corruption involved in incorporation by special legislative act. Throughout the nineteenth century, there was strong popular hostility to corporations in general, and to incorporation by special act in particular. Washington was no exception. Dolliver, "*Condemnation, Credit, and Corporations in Washington: 100 Years of Judicial Decisions - Have the Framers' Views Been Followed?*" 12 U PUGET SOUND L REV 163, 190-195 (1989).

This practice conferred special favors, and was thought to have a bad influence upon legislation. When our constitution was formed it was provided that no corporation should be created by special act of the legislature. The words of the constitution are, "Corporations may be formed under general laws, but shall not be created by special laws, except for municipal purposes. All laws passed pursuant to this section may be altered, amended or repealed, but not so as to impair or destroy any vested or corporate rights." *Oregon Cascade R.R. Co. v. Bailey*, 3 Or 164, 172-3 (1869).

During the nineteenth century, most states enacted constitutional provisions prohibiting incorporation by special act. H.W. BALLANTINE, BALLANTINE ON CORPORATIONS 36 (1946). Article XII, Section 1 of the Washington Constitution, adopted in 1889, prohibited the Washington Legislature from forming corporations by special act. This provision remains in the Washington constitution today.

C. Early corporation statutes were restrictive.

The early general corporation statutes were very restrictive, severely limiting a corporation's maximum capitalization and powers. Gradually, these statutes liberalized as states competed for incorporation fees and taxes. A detailed history of these early restrictions, and the competition between states, appears in Justice Brandeis' dissent in *Liggett Co. v. Lee*, 288 US 517, 549-564 (1933).

D. The first modern statutes.

Outside of a few states which were competing for revenues through liberal corporation statutes, most states continued to have antiquated corporation laws into the twentieth century. In the late 1920's, several states began modernizing their statutes. In part, this was due to a lessening of public hostility against corporations. But in large measure, it was due to states eyeing with envy the revenues generated by liberal states such as Delaware and New York, often from fees paid by corporations back home.

Between 1927 and 1932, nine states modernized their corporation statutes. Garrett, *Model Business Corporation Act*, 4 BAYLOR L REV 412 (1952). Illinois enacted its new corporation statute in 1933, a statute which was a major step in modernizing corporation law.

E. Model Acts & Washington law.

Modern corporate law has been influenced by several uniform or model corporation acts.

The Commissioners on Uniform State Laws published the Uniform Business Corporation Act in 1928. 1 FLETCHER CYC CORP § 2.10 (Perm Ed 1999). In 1933, Washington adopted a corporation act modeled on the 1928 Uniform Act and Washington's new act became effective on January 1, 1934. Ayer, *The New Washington Business Corporation Act*, 8 WASH L REV 97 (1934); Ayer, *The New Washington Business Corporation Act, Part II*, 9 WASH L REV 1 (1934).

However, this Uniform Act did not gain widespread acceptance in the United States. It was adopted by only the states of Washington, Louisiana, and Kentucky and, in part, by Idaho. Hamilton, *Reflections of a Reporter*, 63 TEX L REV 1455, 1457 n 16 (1985). This Act was withdrawn as a "uniform act" in 1943 and renamed the "Model Business Corporation Act." *Id.* at 1457.

At about the same time, the American Bar Association began to develop its own version of a Model Business Corporation Act. In 1946, the Committee on Corporate Laws of the American Bar Association published the Model Business Corporation Act. *Comment*, 39 NEV L REV 575, 576-7 (1960).

The ABA Model Act was adopted in more than 35 states and major portions of it were adopted in other states. Introduction,

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REVISED MODEL BUSINESS CORPORATION ACT XVII (1985); *Equipto Division Aurora Equipment Co. v. Yarmouth*, 134 Wash 2d 356, 950 P2d 451 (1997)(citing this book). In 1958, the Commissioners on Uniform State Laws withdrew their version of a Model Act. Hamilton, *Reflections of a Reporter*, 63 TEX L REV 1455, 1457 (1985).

The ABA Model Act, a second draft of which was published in 1950, was modeled on the 1933 Illinois Business Corporation Act. *Jackson v. Nicolai-Neppach Co.*, 219 Or 560, 348 P2d 9 (1959); 1 FLETCHER CYC CORP § 2.20 (Perm Ed 1999). Revisions occurred in 1957 and 1959, with a substantial revision occurring in 1969. *Id.* Washington adopted most of the ABA Model Act in 1965, with an effective date of July 1, 1967. For a discussion of the 1965 law with prior Washington corporation law, see: Comment, *Model Business Corporation Act*, 38 WASH L REV 538 (1963); Kummert, *The Financial Provisions of the New Washington Business Corporation Act*, 41 WASH L REV 207 (1966); Kummert, *The Financial Provisions of the New Washington Business Corporation Act, Part II*, 42 WASH L REV 119 (1966); Kummert, *The Financial Provisions of the New Washington Business Corporation Act, Part III*, 43 WASH L REV 337 (1967).

More recently in 1984, the Committee on Corporate Laws of the Section on Corporation, Banking and Business Law of the American Bar Association adopted the Revised Model Business Corporation Act. This book sometimes refers to this Act as the "Revised Model Act" and sometimes as "RMBCA."

Washington substantially revised its corporation law in 1989, basing the new Washington act primarily on the 1984 Revised Model Act. *Equipto Division Aurora Equipment Co. v. Yarmouth*, 134 Wash 2d 356, 950 P2d 451 (1997)(citing this book); Maurice, *The 1990 Washington Business Corporation Act*, 25 GONZAGA 373 (1990). The new Washington Act became effective July 1, 1990. Amendments were adopted in 1991, 1994, 1995, 1996, 1997 and 1998. In this book, the Washington corporation laws enacted in 1989 (and effective in 1990), together with all subsequent amendments, will be referred to as the "Act," the "current Act" or the "1990 Act."