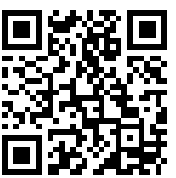

CORPORATION LAW

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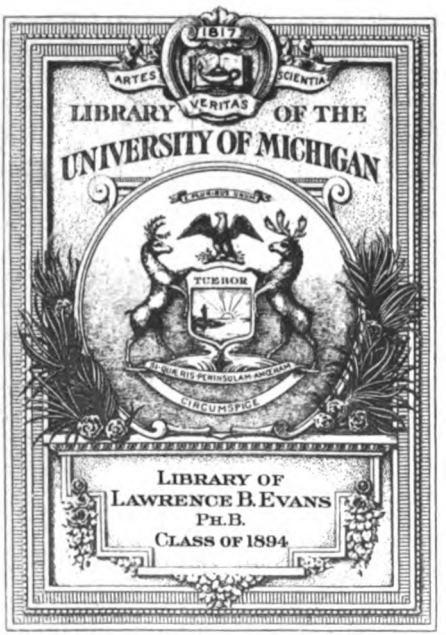

CORPORATION LAW

A COMPREHENSIVE TREATISE ON FEDERAL AND STATE LEGISLATION RELATIVE TO PRIVATE AND PUBLIC SERVICE CORPORATIONS AND INTERSTATE COMMERCE

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INTRODUCTION

THE creation of the modern corporation—"big business," as it is familiarly called—has by its very complexity, by the existence of the wheels within wheels in the body corporate, demanded and brought forth within a comparatively short time a large amount of legislation of greater or less importance. The simple dealings of yesterday between small business firms or between individuals have expanded through the development of the corporation into transactions limited only by the circle of the globe, and consequently there has been created the necessity for effective restricting and controlling influences. The builder of a house in the country, by virtue of his isolation, can make his dwelling about as he chooses, but in the city he is limited by strict building rules and regulations which are imposed upon him in the interest of the many individuals and property which are hemmed in so closely about him. Just so in a large corporation we find the legal situation complicated by the magnitude and scope of the transactions as well as by the relations of the individuals to each other and to the state and nation.

¶ Of course the corporation as a system of business machinery is not necessarily always of the first magnitude, as the idea has been used by business men with large or small capital in cities and towns everywhere. It has come about, therefore, that Corporation Law is of keen personal interest to many nonprofessional people as well as to the lawyer. Each stockholder, director, or officer of a corporation wants to know his rights and duties in the corporation of which he is a member. The stockholder, for his part, wants to know just when he can legally interfere with the conduct of the directors, and how his liability differs from the liability of a director. Each

shipper or railroad man is interested in the reasons for the rule in the Law of Common Carriers that a railroad company is absolutely liable for the loss of goods except through the act of God, a public enemy, or the shipper's own negligence. Furthermore, the recent prosecutions and dissolutions of the so-called "trusts" have focused the attention of lawyer and layman alike on the workings of that anti-trust weapon, the Sherman Act, which has resulted in more than idle interest in the question whether the governmental control would be sufficient to regulate some of the abuses and injustices created by the tremendous growth of the corporation of today.

¶ The present work is a rare combination of ideas by men of exceptional training in this broad subject. The articles were written especially for the American School's correspondence course in law, and the great care which has been taken to make every statement clear renders them valuable not only to the lawyers, but also to those readers who are merely interested in the subject itself. The "trust" phases of the subject and the workings of the Sherman Act are discussed in the articles on "Interstate Commerce Law" and "Anti-Trust Legislation".

PART I

PRIVATE CORPORATIONS

CHAPTER I

NATURE, DEFINITION AND CLASSIFICATION OF CORPORATIONS

§1. Origin and Growth of Corporations. The idea that an aggregation or group of natural persons might, under authority from the State, form an artificial or juridical person possessing many of the powers of the persons composing it, and other rights and privileges apart from these in addition, has been recognized by the courts and lawmakers from the earliest period. Such an artificial or juridical person is known as a corporation, the word being derived from the Latin corpus, meaning a body, as compared with the word animus, meaning the spirit or soul.

Corporations were mentioned in the twelve tables, the earliest known codification of Roman law. The rights of these juridical persons were discussed and fixed in the codes of Justinian, and it is needless to add form an essential part of modern law. The corporate form was limited at first to political or governmental organizations, but in Rome, before Christ, corporations were organized for many private objects, and encouraged or hindered in their organization and activities as best suited the purpose and policy of individual rulers at particular times. Aside from governmental organizations, their development and growth during the earlier part of the Middle Ages was limited, but in the latter part of this period a great commercial awakening led to the establishment of some of the greatest

of corporations, which engaged not only in the conduct of their own business, but also in the control of nations. The Hanseatic League was essentially a corporation which sought to gain commercial privileges through political influence. The East India Company, chartered under Elizabeth; the Merchant Adventurers of London, founded in the twelfth century; the Hudson Bay Company, founded in 1670; the Bank of England, chartered in 1649; the Bank of Genoa, as early as 1407, and the Hamburg Company, in 1248, are interesting and historical illustrations of the advantages gained by natural persons making use of the legal idea of a juridical person. It is unnecessary to refer to the tremendous development and increase of corporations, especially private, during the nineteenth century.

§ 2. **Definitions.** The best known definition of a corporation is that given by Chief Justice Marshall:[1]

"A corporation is an artificial being, invisible, intangible, and existing only in the contemplation of law; being the mere creature of the law, it possesses only those properties which the charter of its creation confers upon it either expressly or as incidental to its very existence."

Another definition prepared by Austin Abbott for the Century Dictionary is more concise:

"An artificial person created by law or under authority of law from a group or succession of persons and having a continuous existence irrespective of that of its members, and powers and liabilities different from those of its members."

An interesting definition by the late Jay Gould, although not legally accurate, illustrates well the popular public conception of a corporation. He defined one as:

"A body of men who unite, associate and concentrate their ability, capital and intelligence in the undertaking of a work, great or small, which any one of them would individually be unwilling to undertake. If there are losses, they agree to pay each his proportion; if there are profits, they agree to divide them."

[1] Trustees of Dartmouth College v. Woodward, 4 Wheaton (U. S.) 518.

From these definitions, the nature of a corporation clearly appears and the purpose of their organization is indicated in the definition of Jay Gould. Stated briefly, the commercial use of the private corporation is chiefly for the resulting convenience, economy, unity, and continuity in the transaction of business or management of property. Certain powers and functions can be exercised better by an artificial body than by a number of natural persons, and the State may better exercise over this collective body, this artificial person, its rights of control and regulation, than over a number of individuals. Great and advantageous economies in business can be effected by combinations of energy and capital. The development of the modern commercial world, as it exists today, would have been impossible but for the notion of a juridical person, the corporation.

§ 3. **Nature and Power.** The Roman idea of a corporation was an entity personified. A collection of individuals as opposed to the idea or notion of a *singularis persona.* The next development in respect to the nature of a corporation is to be found in the common law. This system emphasized the idea of a corporation as an artificial person; a legal entity distinct and separate from the members of the corporation, and this idea prevails at the present time, except so far as it has been modified by modern decisions which will be noted later. The early English judges and legal authors referred to the corporation as an artificial person, a being without a soul and incapable, therefore, of committing torts or crimes. Alluding to corporations, Lord Coke wrote, quoting from Manwood, J.:

"No one can create souls but God; but the king creates corporations, and, therefore, they have no souls."

The common-law conception of a corporation as a distinct legal entity has been modified in modern times by the idea that in a corporation there exists certain elements which are purely manifestations of law, and also certain physical characteristics which are independent of law, namely, a membership of natural persons. Courts of law regard a

corporation as a distinct and legal entity apart from its members for the purpose of the transaction of its business in every detail. Courts of equity, however, in order to render substantial justice, regard a corporation not only as a legal entity, but also in its true light as an artificial person, composed ordinarily of natural persons.

In order to emphasize some of the essential characteristics of corporations they can be compared with a copartnership, another form of individual association or combination, and with natural persons. These essential characteristics, as thus compared, are, first, the idea of immortality; the corporation exists for the time limited in the charter, irrespective of the individual lives of those who may compose it; its powers and rights, its duties and obligations remain the same, though its members may be constantly changing; it is a legal person distinct from its members. The second characteristic is that in a corporation, in the absence of statutory or constitutional provisions, the members are not personally liable for the corporate debts. Each member of a partnership, on the other hand, is individually liable for the debts of the firm, and natural persons, *sui juris,* are liable to the fullest extent for obligations contracted by them. In a corporation, the liability of the individual members who compose it, is limited and is merged into or lost in the legally responsible person.

§ 4. **Classification and Basis.** In order to understand the powers and rights of corporations, and also their liabilities and responsibilities, it is necessary to learn their classification and its basis. The most important division of corporations is based upon the functions performed, that is, the legal characteristics of their powers and rights, whether exercising governmental powers, performing governmental duties, or engaged in the conduct of an enterprise having for its object the personal and individual gain of the members of the corporation. Under this classification we have public, private, and quasi-public corporations. Public corporations are those created by the sovereign power or state as aids to it in performing and exercis-

ing its governmental functions and powers. They are regarded as governmental agencies and include counties, school districts, road districts, towns, villages, cities, park boards, and other organizations of a similar nature. A private corporation is one created for the conduct and carrying on of a private enterprise or business, designed solely for the personal and usually the pecuniary gain or emolument of the individual members, and does not, nor can it, partake of the nature of a public corporation. There are other corporations which are technically and essentially private, engaged in some private enterprise but in which the public interests are indirectly involved to such an extent as to give the State the right of exercising a greater degree of control and regulation than is consistent or usual in the case of an ordinary private corporation. Familiar illustrations of quasi-public corporations are: railroad, express, elevator, street railway, telephone, and telegraph companies, and corporations organized for the purpose of supplying water and light to municipalities. The primary and direct objects of private corporations are to promote private interests in which the public has no concern except the development of the general resources of the country. They derive nothing from the State except the right of corporate existence and to exercise the powers granted.

Another classification of corporations is based upon the number of members and the terms used here are aggregate, indicating a membership of many and sole implying a membership of but one. There are few corporations sole in the United States. They are usually religious organizations represented by a church official to whom corporate power is given and who constitutes the corporation. Corporations may be also classified according to the purpose of their organization, whether religious in their character as ecclesiastical, or purely civil in their nature as lay. There are also many miscellaneous classifications, generally statutory or constitutional. The purpose of the division being the grant of particular powers to one class of corpora-

tions and not to others; in other instances a difference in methods of taxation or a variance in State control in still others. They are also divided into stock and non-stock corporations, the first having capital stock, so called; domestic, foreign, and alien, a division based upon the viewpoint of a particular State; a domestic corporation being one created and existing under the laws of that State. A foreign corporation is one created and existing under and by virtue of the laws of another State, and an alien corporation is one created by virtue of the laws of an alien or foreign sovereign. In some States the term domestic by statute is made to apply to corporations created under its laws, and the word foreign refers or applies to all corporations created under the laws of another State or country.

CHAPTER II

CREATION OF CORPORATIONS

§ 5. By What Authority. Individuals cannot, as a matter of right, assume the form and powers of a corporation. These bodies possess powers which can only be created by the sovereign State and which, therefore, cannot be assumed at will by any group of natural persons. Before a corporation can, therefore, be organized, there must exist affirmative action on the part of the sovereign authorizing this to be done. The power to create a corporation is lodged, in this country, in the law-making branch or department of government of either of the several States or of the United States. In foreign countries, controlled by one sovereign, no controversy exists as to where the power to create corporations is to be found; but in the United States, where there exists a dual sovereignty, viz., the United States of America and each of the different States, the question early arose as to the power of these respective sovereignties to create corporations. It was conceded that as each of the separate States was independent and sovereign, exercising all of the powers not specifically or by fair implication granted to the Constitution of the United States, that they could freely exercise the right of creating corporations, except as limited by the Federal Constitution. The doubt of right existed in connection with the power of the Federal Government to create a corporation, and this was denied by those attacking its exercise upon the basis of a strict interpretation of the Federal Constitution. The Federal Government is one of delegated powers, and it was claimed that nowhere in the Constitution, the instrument creating it, could be found a clause directly or expressly giving the power to create a corporation. In McCulloch v. Maryland,[1]

[1] 4 Wheaton (U. S.) 316.

the question was decided in favor of the existence of the right. In this case the validity of the organization of the Bank of the United States was raised. The power to create this or any other corporation was denied, but Chief Justice Marshall, in his opinion, held:

"The power of creating a corporation, though pertaining to sovereignty, is not like the power of making war or levying taxes or of regulating commerce, a great substantive and independent power which can be implied as incidental to other powers or used as a means of executing them. It is never the end for which other powers are exercised, but as a means by which other objects are accomplished."

The court also, in the course of its opinion, held that even if the general clause of the Federal Constitution giving Congress the power to pass all necessary and proper laws for carrying its powers into execution did not give the power to the Federal Government to create a corporation, it would still possess this power, for the grant of a power always and necessarily implies the grant of all usual and proper means for its execution. As a means to this end, therefore, and for the purpose of carrying out or of executing some power belonging to the Federal Government, it may, therefore, create corporations; and since the McCulloch case this power has been frequently exercised and has never been denied.

§ 6. **Manner of Creation.** Corporations may be created through the direct and affirmative action of the sovereign state, or in some cases by indirection. The acts of a law making body are known as general or special. A general act or law has been defined as:

"A statute which relates to persons or things as a class, while a statute which relates to particular persons or things of a class is special."

The mere arbitrary grouping, classifying or arranging of certain objects will not, of itself, make legislation gen-

eral. There must be a logical basis for the desired effect, independent of conditions or circumstances then existing. In another case the distinction was noted in the following language:

"A law is general in the constitutional sense which applies to and operates uniformly upon all members of any class of persons, places or things requiring legislation peculiar to itself in matters covered by the law; while a special law is one which relates and applies to particular persons of a class, either particularized by the express terms of the act or separated by any method of selection from the whole class to which the law might, but for such limitation, be applicable."

It was the universal practice at first to authorize the creation of corporations by either general or special acts or laws, but the inherent vice of special legislation led almost universally to the adoption of constitutional provisions in the different States prohibiting the creation of corporations by laws of that character. Where no such constitutional provision exists, corporations may be created, as already observed, by laws or acts of either class. Where, however, such constitutional provisions do exist, the manner of creating a corporation is limited to the general laws passed by the legislature relating to and providing a common method and procedure.

Through Indirection. Corporations may be also created through indirection, or by the absence of affirmative action on the part of the sovereign State. There are two ways recognized by the courts in which this may be done, viz, through the application of the doctrines of prescription and implication. A corporation is said to exist by prescription if its origin cannot be shown, and in such a case the law presumes, through the lapse of time, that the corporation came into existence through or by an act of the sovereign. This doctrine is applied more frequently to public corporations, but in some instances private corporations have been held to be thus created.

By Implication. As no particular form of words is necessary to create a corporation, but rather the existence of an intent on the part of the sovereign to so act, it has been held that where a body of men, acting as a corporation, have been recognized as such in some law or by some direct act of the sovereign, that there is impliedly created a corporation. This doctrine also has been applied more frequently to public corporations than private, but instances of its use in respect to the latter have been found. It might be said, however, that the doctrines of prescription and implication are seldom applied at the present time. The different States have provided either general or special laws under which corporations may be created, and, as will be noted later, one of the essentials of a legal corporation is a substantial compliance with their provisions.

§ 7. Constitutional Limitations. One constitutional limitation upon the power of the law making body to authorize the creation of corporations was noted in the preceding section, viz., a constitutional prohibition against the passage of special laws. In addition, there will be found further limitations in all constitutions upon the power of legislative bodies as to the manner and the form of their action. These limitations apply equally to legislation in respect to corporations as to other subjects. The reader must refer to the Constitution of his own particular State in order to be correctly informed as to the extent and the character of such restrictive provisions, but one or two may be suggested which are commonly found. Laws, as a rule, must be uniform in their operation throughout the State; that a bill deals with only one subject and that the one expressed in its title, is another constitutional requirement which may be urged against legislation looking to the organization or the control of corporations. There are many others, but only the suggestion of their existence is permissible at this time.

§ 8. Organization under General Laws. Justice Story said, in the Dartmouth College case, that the creation of corporations unquestionably resulted in an advantage and

benefit to the community at large, and because of this well recognized result it is the policy of all States to encourage their organization, and general laws are to be found under which exists, as a rule, the greatest freedom of action by individual persons in this respect. These general laws provide in detail the acts required to be done by those desirous of organizing or forming private corporations. They may include a classification either based upon the powers to be exercised by the corporation, or some right of the State in respect to the nature and extent of its control over them. Definitions are also given of the phrases and words used, and such preliminary provisions as will enable the incorporators to ascertain the steps required.

§ 9. Steps Required for and Essentials of Legal Incorporation. The requirements in the States differ, but it is generally necessary to include in the articles of incorporation paragraphs or sections relating to the name of the corporation; the general nature of its business and the principal place of transacting the same; the period of its duration, if limited; the names and places or residence of the incorporators; the board of management, with its powers; the date of its annual meeting, and the names and addresses of those composing this board until the first election; the amount of capital stock, if any; how the same is to be paid in; the number of shares into which it is to be divided; the par value of each share and the methods of voting thereon; and the highest amount of indebtedness or liability to which the corporation shall at any time be subject. There is usually no limitation upon articles of incorporation containing also other lawful provisions defining and regulating the powers or business of the corporation, its officers, directors, members, or stockholders. These articles of incorporation, when executed by the incorporators in the manner provided by law, are required usually to be filed with the Secretary of State or some other designated officer, the fees fixed paid and then published in the manner designated by law in some newspaper and recorded in the office of the Register or Recorder of Deeds of the county in which its

principal place of business is located, or some officer performing equivalent duties. It is also necessary, as these various steps are taken, to have the proper official certify, in the manner provided, as to his official acts.

Incorporators, Name, and Seal. It will appear later that the relation which exists as between the corporation and the State, and the members of the corporation, is a contract one, and it is necessary, therefore, that the incorporators should be persons *sui juris,* or those legally competent to enter into the contract relation. The number also of incorporators or those signing the articles of incorporation cannot be less than fixed by statute. This number will vary; for the purpose of organizing corporations of certain classes a larger number may be required than in the case of others.

The incorporators are not permitted to adopt any name they please, but are limited, as a rule, to that name which will distinguish it from all other corporations, domestic or foreign, authorized to do business within the State of its creation, and the word company, corporation, or incorporated, is usually required to be added to indicate the fact that it is an incorporated association or corporation. In some States assuming a corporate name or one suggesting corporate existence, without actual incorporation, is made unlawful.

The corporate name and its use after adoption is protected by law, and many decisions will be found holding that corporations organized under the laws of different states cannot adopt or use a name similar, where their business is interstate and general and of a like nature, as to cause confusion in the use of the name; or where a later company adopts a name already in use by some well known corporation and which is adopted for the evident purpose of availing itself of the reputation and business of the company already organized.

Corporations are usually required by statute to provide a seal bearing the name, and, in some instances, the date of incorporation. Statutory provisions also may require, in

many instances, the use of this seal by the proper officer of the corporation in order that a particular instrument may be regarded as legally acknowledged or entitled to record in the offices of recording officials. Formerly the rule adopted by the courts was that the corporation "spoke through its seal." This doctrine required its frequent use, and further involved the idea that unless the seal was affixed to the written acts of the corporation they were not legally executed, and, therefore, incapable of enforcement; or that no legal rights arose or were created because of or through the execution of the particular instrument in question. This strict rule has been materially modified in recent years, and it is only where statutory provisions require the affixing of the seal that a failure to use it will lead to the legal results above indicated. It is the safest procedure, however, for the corporation to have its seal affixed on all formal instruments or contracts which it may execute or make.

Essentials of a Legal Corporation. From what has already been written and from what will appear later, it is clear that a corporation is a legal entity or artificial person, distinct and separate from its members, having powers and liabilities also separate and distinct from those of its members. That the liabilities and obligations of the members of the corporation are different from their obligations and liabilities as natural persons, or as members of a partnership, or other association of natural persons. It cannot be too emphatically stated that this liability is a limited one. The liability of a member of a firm—unless one is a special partner—is only limited by the extent of the debts of the firm. His personal estate may be taken to liquidate the debts of the partnership. The liability is a personal one. The liability of a natural person, *sui juris* (of his own right) for his debts is also a personal one and only limited by their extent. It may be, therefore, very important to determine the exact legal status of an association of persons whether a corporation or some other form of organization. To ascertain when a legal or *de jure* (of right)

corporation exists, the courts have held that certain essential facts must be found, and these are commonly known as the tests of legal incorporation.

Grant from State, and Acceptance. The first of these essentials is the existence of a grant or offer on the part of the State under which a corporation may be organized; or, as some cases have expressed it, a legislative grant is necessary. This is essential because a corporation exercises powers and capacities different from those of a natural person or any other form of association or natural persons other than a corporation. The powers enjoyed by corporations are very frequently those which cannot, because of the nature of things, be possessed or exercised by natural persons, as, for example, the capacity of immortality. Not only must there exist a legislative grant on the part of the State, under which corporations may be organized, but there must also be an acceptance of this grant by those desirous of organizing a corporation. This acceptance is usually evidenced by the execution of the articles of incorporation, the organization of the corporation and the transaction of business by it in its corporate capacity. This essential or test of a legal corporation is necessary because of the contract relation existing between the members of the corporation and the State. The State cannot compel natural persons to organize a corporation or undertake the business of conducting one. In this respect the principle is totally unlike that which applies to the public corporation. In the organization of public corporations, the State can arbitrarily force upon the people of a particular locality a form of organization or a local government having for its purpose the assumption and exercise of governmental powers and functions. No acceptance by the persons to be affected is necessary. A private corporation, however, is, in its nature, radically different from that of a public corporation. It is organized for totally different purposes and results. The public corporation, from the standpoint of the persons affected, is an involuntary organization. The private corporation is the result of a purely voluntary act

by those desirous of organizing it. If no acceptance, therefore, of the grant or offer of the State to organize a private corporation, by those constituting the alleged corporation, can be shown, one of the essential tests has failed, and that particular body of men will not be regarded as a legal corporation.

Agreement between Members. Because of the contract relation which exists not only between the State and the corporation, the State and the members of the corporation, and also between the members of the corporation, or as among themselves, it is necessary that there be an agreement or understanding between those organizing a corporation that this is the nature of their act. If one of the incorporators understands that the instrument he is signing is a conveyance of real property instead of articles of incorporation, the meeting of the minds necessary to the making of a legal contract is wanting, and another of the tests of a legal incorporation has failed.

Compliance with Statutory Provisions. There must also be a substantial compliance with statutory requirements in order that a legal corporation may exist. "A substantial compliance with all the terms of a general incorporation law is prerequisite to the right of forming a corporation under it." It is necessary that the required number of incorporators sign the articles of incorporation. The law authorizing the incorporation of corporations may contain provisions mandatory or merely directory in their nature. These terms are self-explanatory. The principle of law in respect to mandatory provisions is that not only must there be a substantial but even a strict compliance, and this is especially true where certain conditions precedent to legal incorporation, as they are termed, are required by the statutes. A strict compliance with the provisions of the law which are merely directory in their character is not necessary, and there may be a variance or an immaterial irregularity in following them which will not affect the legality of the corporation. These irregularities or informalities afford, as a rule, no basis for an attack upon the

legality of the corporation by third persons. The State alone can take advantage of them if it so desires, and even the State may be barred from such proceedings by lapse of time. The signing of the initials instead of the full Christian name to the articles of incorporation; the statement that "said corporate stock shall consist of five hundred shares at one hundred dollars per share" when the statute required that the certificate of incorporation "shall state the amount of capital stock"; the statement that the corporation shall exist "at least forty years" when the statute provided that the certificate should state "the term of existence not to exceed forty years," are illustrations of irregularities which will not affect the legality of the organization.

The statutes may, however, contain provisions which are intended to be conditions precedent to incorporation, for example, the execution of the articles of incorporation. These are usually regarded as mandatory and must be strictly complied with before a legal corporation can exist. The intent of the law in this respect must be gathered from its language, and no general rule can be stated which will enable one to determine what are intended to be conditions precedent and, therefore, mandatory as to compliance with them, and what are regarded as general provisions of the law or those which are merely directory, and in respect to which a strict compliance is not necessary.

§ 10. **The Doctrine of Collateral Attack.** Since it is the State which alone creates the corporation, and not third persons who may have dealings with it, the doctrine of collateral attack, as it is termed, is universally followed by the courts. The presumption of law is that the corporation has been legally and regularly organized and that it is a legal incorporation. All that is necessary, therefore, except in direct proceedings by the State in which the main question or issue is the legality of the corporate existence, is that the corporation establish its character as a *de facto* corporation, or one existing in fact, although possibly not in law. All that is necessary to be shown is that there is

a valid law under which such a corporation might have been organized; an attempt in good faith to incorporate under the law; a colorable compliance only with the provisions of the law, and an exercise of corporate powers in a corporate capacity. The subject of *de facto* corporations will be considered later.

§ 11. Corporations as "Citizens" or "Persons". In an early case in the United States Supreme Court, Bank of Augusta v. Earle,[1] it was decided, and the doctrine has never been denied, that a corporation, for the purpose of jurisdiction, was a citizen of the State under the laws of which it was created. The stockholders are arbitrarily held to be citizens of that State, and the fact of their diverse citizenship, therefore, will not affect the citizenship of the corporation. Even where a corporation doing business in several States has been organized under the laws of the different States by the same name, the rule is not changed. This principle is nearly axiomatic, as the laws of the different States can have no extra-territorial effect. When the term "citizen of the United States" or "citizen" is used in the Federal Constitution, it has been held that a corporation is not a citizen; but in the fifth and fourteenth amendments, where the term "person" is used in connection with several prohibitions against the States having for their object the protection of personal and property rights, the courts have held that corporations are persons within the meaning of the term as there used, and that they, therefore, come within the protecting provisions of these amendments, that no State can pass any law depriving any person of property without due process of law, nor deny to any person within its jurisdiction the equal protection of the law.

Corporations, as a rule, are deemed persons within the meaning of State statutes when the circumstances in which they are placed are identical with those of natural persons who are included within the operation of the statutes.

[1] Bank of Augusta v. Earle, 13 Peters (U. S.) 519.

CHAPTER III

PROMOTION OF CORPORATIONS

§ 12. Definition of Promoter. It is difficult to give an exact definition of the word promoter, as the relation which is indicated by the word depends upon the character of the acts done in each particular instance. The law imposes serious responsibilities upon those who engage in the organization and promotion of corporations and holds them substantially to the position of a trustee for the benefit of all those who may be directly involved in the undertaking. The term has been defined as "one of accepted use commonly employed to designate persons who take some part in procuring the promotion of a corporation by inducing others to join it, and who, in so doing, assume such a position that a relation of fiduciary nature between these and the corporation is created." From this definition and from the nature of the question it will be readily seen, as already suggested, that the relation is one depending upon the character of the acts done.

§ 13. Fiduciary Position of Promoters and Secret Profits. Since the law has well established the fiduciary or trust position of a promoter to the corporation and others directly interested in it or its organization, it necessarily follows that promoters cannot take personal advantage of their transactions or acts done in connection with the organization of the corporation to its detriment or to the detriment of its members, and this rule is especially applicable where those who are entitled to act for the corporation have no knowledge or information in respect to the profits, commissions, or other advantages which may be derived by the promoters from their transactions in promoting the corporation. If any agreements or contracts, by which the promoters receive special advantages or

profits, are disclosed to those entitled to act for the corporation and its members, and their assent obtained, the rule is not so strictly applied, unless the profits or commissions are exorbitant or unconscionable, promoters, therefore, it is universally held, must account to the corporation for all secret profits, commissions, or bonuses which they may receive in connection with the purchase for or the sale of property to the corporation. They may also become liable to the corporation for their acts of a fraudulent nature, or for their misrepresentations under the same circumstances as individuals who are not promoters would be liable. The corporation may, by means of the proper proceedings in a court of equity, by or for its benefit, recover secret profits or commissions, or, at its election, rescind a sale of property to it and recover the consideration paid therefor.

§ 14. Personal Liability of Promoters. The acts of promoters are usually done in furtherance of the organization of a corporation not yet in existence. Their contracts and transactions are made for and in behalf of an artificial person not yet in existence. It may, as a matter of fact, never be fully and completely organized so as to become even a *de facto* corporation, that is, one existing in fact but not a strictly legal entity or *de jure* corporation. The question, therefore, frequently arises of the liability of the corporation when it is legally organized, upon the contracts or agreements of the promoters previously made for the benefit of the future corporation. In England, the rule is that in the absence of statutory or charter provisions, a contract made under such circumstances by the promoters is a nullity and that the corporation cannot ratify or adopt it thus making it its own after incorporation, although if it accepts the benefits of such a contract an action *quasi ex-contractu* (as if on a contract) may be maintained against it. This doctrine is also followed by the Supreme Court of Massachusetts.[1] The English doctrine, however, has been substantially repudiated in all the other States. The personal liability of the promoters

[1] Abbott v. Hapgood, 150 Mass. 248, 22 N. E. Rep. 907.

on contracts made before incorporation will depend largely upon the question of the intent of the parties to the contract. If it is understood or agreed that the other party shall look to the proposed corporation alone, the promoters are not, as a rule, personally bound by the terms of the contract, but, in the absence of such an understanding, or of such an intent, as shown by the facts and circumstances surrounding the making of the contract, they will be personally obligated. If, however, the corporation, later, upon its formation, assumes or adopts the contract, and the other party to it consents, there is then a novation of the parties and the promoters will be relieved from any personal liability. If such consent is lacking, however, the liability still attaches to the original parties to the contract. If they are personally bound, it follows, necessarily, that they can enforce the terms of the contract in an action thereon in their own name.

§ 15. Liability of the Corporation on Promoters' Contracts. It has already been stated in the preceding section that the rule in England and in Massachusetts relieves the corporation from any liability on the contracts of its promoters, although, if its benefits have been received and accepted by the corporation an action *quasi ex-contractu* may be maintained by the corporation upon it. The overwhelming weight of authority is, however, that a liability for the obligations of a contract may be and is shifted from the promoters to the corporation, not only by an acceptance of the benefits as above stated, but also if there is an express assumption by the corporation of the contract, in which case there will arise a novation between the parties; or, if the corporation, acting through its proper representatives, formally ratifies the contract. To summarize: it will be seen that the burden of the promoter's contract made before the organization of the corporation, or on behalf of the corporation, in existence but not yet engaged in the transaction of its business, may be shifted from the promoter as one of the parties to the corporation when the corporation accepts the benefits of the contract, formally assumes or

adopts it, or legally ratifies the act of the promoter in making the contract for its benefit. In the latter case, the corporation formally recognizes the promoter as its agent and ratifies his acts on its behalf previously done without authority. It is true that no relation of agency can exist between a promoter and a principal not yet in existence, and subsequent action by the corporation is necessary to make it liable for the private acts of the promoters.

§ 16. **Fraudulent Acts of Promoters.** Neither the corporation, when it is subsequently formed, nor subscribers for its stock, will be bound by the fraudulent acts of promoters. If the subscriptions are obtained through fraudulent representations made either orally or in writing, the one who is misled may recover the resulting damages from the promoters. This rule does not depend upon the fact that the misrepresentations or untrue statements of material facts may not be made to the subscribers of the stock personally. It is sufficient, in this country, if the statements, the natural tendency of which is to deceive and mislead and to induce those who read them to purchase the stock, are made or contained in circulars, advertisements, prospectuses, or other published matter issued for the purpose of obtaining subscriptions, and on the faith of the statements contained in them the subscriptions were so made.

§ 17. **Expenses and Services of Promoters.** Promoters, in organizing a corporation not yet formed, frequently incur heavy expenses and render services, payment for which they subsequently seek to recover from the corporation. The courts have held that the legitimate expenses of organization and a reasonable value for their services may be recovered, but extravagant claims for services, unnecessary or illegitimate expenses, are usually disallowed. In case of a failure to organize a corporation, the promoters, as a matter of course, are liable, personally, for expenses which they may have incurred, and they are also liable, in addition, for moneys which may have been received from subscribers to the stock of the proposed corporation as a

deposit or a preliminary payment on account of their subscriptions. As to the latter, if there is no understanding between the subscribers and the promoters, the moneys so received must be repaid in full to the original subscribers, and a proportionate part of the expenses of organization can not be retained by the promoters. If, however, there is an understanding or agreement by subscribers that they shall bear their proper share of the expenses of organization, including disbursements and the value of the services of the promoters, these are a proper charge against the moneys so paid in and no action will lie for a recovery of sums so retained.

CHAPTER IV

QUESTION OF LEGAL EXISTENCE HOW AND BY WHOM RAISED

§ 18. De Jure and De Facto Corporations. The terms *de jure* and *de facto* have already been used in a preceding section, and a brief discussion of what is understood by them will be given in this chapter. A corporation, it will be remembered, is a distinct artificial person, a legal entity, created by the sovereign or under its authority, exercising powers and possessing capacities not belonging to a natural person or group of persons other than a corporation. The State, speaking of it as a sovereign power, alone has the authority to create, and by statutory enactment prescribes the conditions and the manner in which a corporation may be organized. When these conditions have been substantially complied with there results a corporation *de jure* which can successfully defend its right to exist in a corporate capacity even against the State. Those organizing a corporation, on the other hand, may fail to comply with statutory conditions to such an extent as to defeat the legal existence of the corporation not against third persons raising the question, but as against the State in a proper proceeding brought by it for that purpose. Such a corporation is known as one *de facto*. What is the attitude of the courts in respect to the regularity of corporate organization when the question is raised? There are two doctrines or theories in this respect, the great weight of authority, on the one hand, holding that where a body of men act as a corporation and in the ostensible possession of corporate powers, it will be conclusively presumed that they are a corporation in all cases, except in a direct proceeding against them by the State to vacate their charter. The other doctrine can be stated

as follows: that conditions precedent must be strictly complied with or the corporation does not exist. The failure can be taken advantage of by anyone in private litigation with the pretended corporation. The common and almost universal legal doctrine is, that in respect to the existence of a legal corporation, the presumption of legality exists. This principle is merely another phase of the doctrine of presumption of right acting. A man charged with crime is presumed innocent until he is proven guilty by the State. One acting as a public official in the ostensible possession of an office is presumed to act under rightful authority and to be legally entitled to perform the duties of the office until the contrary is shown, and the same presumption of right acting operates as above stated. Corporations are presumed to be at least *de facto,* and the further rule holds that the question of their right to corporate existence cannot be raised by third persons engaged in private litigation with them. The term *de facto,* as applied to a corporation, means a body which actually exists for all practical purposes as a corporate body, but which, because of a failure to comply with some provisions of the law, has no legal right to corporate existence as against the State. A corporation *de jure,* on the other hand, is a corporation in law as well as in fact. Not even the State can deprive it of its corporate existence in violation of the terms of its charter.

The doctrine of *de facto* corporations, as it is termed, is based upon the fundamental doctrine that the State alone creates a corporation, and that no third person can question the right of a group of persons, apparently clothed with corporate capacity, to act as a corporation. If the State chooses to ignore a failure to comply with the provisions of laws enacted by it, that is its privilege. In a Minnesota case[1] this reason was well stated:

"The rule relating to *de facto* corporations is not founded upon any principle of estoppel, as is sometimes assumed, but upon the broader principles of common justice and

[1] East Norway Lake Church v. Froislie, 37 Minn. 447-451.

public policy. It would be unjust and intolerable if, under such circumstances, every interloper and intruder were allowed thus to take advantage of every informality or irregularity of organization."

The rule is also based upon the universal principle that a person, to be entitled to maintain a proceeding to question the powers, rights, privileges, and immunities of others, must have some title or legal or equitable interest in the subject in regard to which these exist, or one's rights must be affected. Clearly, third persons dealing with corporations have no right to question the validity of corporate organization in actions where this question is not one which can be regularly raised or is the main issue. The validity of corporate organization cannot be collaterally attacked.

§ 19. Essentials of a De Facto Corporation. To constitute a legal or *de jure* corporation, it is necessary that there exist an offer on the part of the State or a legislative grant, an acceptance of this grant by the incorporators, an agreement between them as to the nature of their act, a substantial compliance with conditions precedent, and the enabling statutes. If these essentials exist the result is a corporation *de jure,* which is secure in its corporate life even as against the State, unless it violate some provision of its charter. To constitute a corporation *de facto,* it is only necessary that there should be found, in the first place, a valid law and one which authorizes such a corporation. To be a corporation *de facto,* it must be possible to be a corporation *de jure,* and acts done in the former case must be legally authorized to be done in the latter or they are not protected or sanctioned by law. The acts of a corporation *de facto* must have an apparent right.

The second necessary condition to the existence of a corporation *de facto* is an attempt on the part of the incorporators, in good faith, to organize under the law. There must be the *bona fide* attempt on the part of those organizing the corporation to take the necessary steps to organize one and to become a corporation. The courts also hold

as a third test of a corporation *de facto* that there must be a colorable compliance with the conditions of the enabling statutes. It will be remembered that a substantial compliance with the provisions of the enabling act or a strict compliance with conditions precedent is necessary to constitute a corporation *de jure.* What is understood as a colorable compliance? The best answer, perhaps, is a quotation from a case.[2]

"When a body of men are acting as a corporation under color of apparent organization in pursuance of some charter or enabling act, their authority to act as a corporation cannot be questioned collaterally. . . . Color of apparent organization under some charter or enabling act does not mean that there shall have been a full compliance with what the law requires to be done when there is a substantial compliance. A substantial compliance will make a corporation *de jure;* but there must be an apparent attempt to perfect an organization under the law. There being such apparent attempt to perfect an organization, the failure as to some substantial requirement will prevent the body being a corporation *de jure.* But if there be user, pursuant to such attempted organization, it will not prevent it being a corporation *de facto.*"

As the last essential of a corporation *de facto,* the courts hold that not only must there exist the conditions previously noted, but that the persons so attempting to organize a corporation must proceed farther; they must proceed to an assumption of corporate powers or corporate user, as the phrase is found. The acts relied upon to show user, must be in their nature corporate acts and not the mere acts of individuals which happen to be not inconsistent with those of an incorporated society.

§ 20. The Powers of De Facto Corporations. A corporation *de facto* is, to all intents and purposes, for the transaction of its corporate business, one *de jure.* It is recognized by the courts as a corporation and not otherwise; its right to so act cannot be questioned collaterally by third

[2] Finnegan v. Noerenberg, 52 Minn. 243.

persons, and it necessarily follows that the corporation can sue and be sued, execute contracts, buy and sell property, exercise the power of eminent domain; in brief, exercise all of the powers that a corporation *de jure* of a similar character or nature might.

§ 21. Estoppel to Deny Corporate Existence. Another legal principle is applied by the courts against third parties questioning the right of a group of persons to exercise corporate powers. This principle may be briefly stated, that persons who transact business or assume contractual relations with what purports to be a corporation are equally with the corporation itself estopped to deny the validity of the incorporation in actions brought to enforce liabilities growing out of such transactions. This principle applies to those holding themselves out as a corporation, the corporation itself and third persons dealing with the corporation. The doctrine of estoppel is based on equitable grounds, and should, therefore, be applied only where there are equitable reasons for relief. It is rarely that this principle is applied, however, as the doctrine of *de facto* corporations, as stated in the preceding sections, is universally followed and is held sufficient to prevent an attack on corporate existence by third persons, the use of the doctrine of estoppel being, therefore, unnecessary. In a Michigan case,[3] the court said:

"Where there is thus a corporation *de facto* with no want of legislative power to its due and legal existence, where it is proceeding in the performance of corporate functions and the public are dealing with it on the supposition that it is what it professes to be; and the questions suggested are only whether there has been exact regularity and strict compliance with the provisions of the law relating to incorporation, it is plainly a dictate alike of justice and of public policy that in controversies between the *de facto* corporation and those who have entered into contractual relations with it as incorporators or otherwise, such question should not be permitted to be raised."

[3] Swartout v. Michigan Air Line R. R. Co. 24 Mich. 390.

§ 22. Organization under an Unconstitutional Law. A common rule of law is that an unconstitutional law is the equivalent of no law, and where an attempted organization has been had under a law which is subsequently declared unconstitutional the attempted corporation will not be regarded as even a *de facto* corporation, and acts done by it will not be regarded or held to be corporate acts. The liabilities and the obligations of the pretended corporation will be considered as the personal liabilities and obligations of its members.

CHAPTER V

THE STATE AND THE CORPORATION ITS CHARTER

§ 23. Visitorial Power. The greater number of private corporations, until within recent years, were of a charitable or ecclesiastical nature, and it was customary for the founder of such a corporation or institution in the organization of the corporation, accompanied generally by a donation of funds for its establishment and maintenance, to provide that a representative, to be selected by him or his heirs, should have the right of "visiting" the institution in order to determine whether the purposes and objects for which it was originally created were being carried out and in a manner in conformity with the original intentions and wishes of the founder. This power of visitation, as it was termed, is, in a historical sense at least, the basis of the right of the State to control and regulate the conduct and the business of private corporations. The deeper reason, as well as the true one, is not derived from the ancient power of visitation, but depends upon the legal proposition that the State creates the corporation and that it alone has this power. All corporations, therefore, assume a corporate existence and engage in the conduct of their business subject to the supreme power of the State to regulate and to control them. This power is only limited by constitutional provisions having for their purpose the protection of fundamental and vested personal and property rights, and since, as will be stated later, the relation between the State and the corporation is a contract one, the power of control and regulation must be exercised in the manner provided by charter and in accordance with the same general principles of law which govern contracts between individuals.

§ 24. Control of Quasi-Public Corporations. In that section containing the classification of corporations, a division was given based upon the nature or character of the functions performed respectively by different corporations, corporate organizations falling within this classification being known as public, quasi-public and private, or, strictly speaking, public and private, the quasi-public corporation being, in all its essential characteristics a private one. The control by the State of public corporations is absolute, except as limited by constitutional provisions. The extent of the power of control of private corporations by the State is indicated in the preceding section.

Quasi-public corporations are private corporations but the conduct of their business affects the interests of the public in a large sense, and for this reason they are subject to a greater degree of control and regulation by the State than other private corporations not falling within this class. It is this fact which gives rise to the designation or term of quasi-public corporations. This principle of greater control and regulation was first authoritatively announced by the Supreme Court of the United States in the so-called Granger cases. The one most frequently cited is Munn v. Illinois,[1] where Chief Justice Waite, in the majority opinion, said:

"Their business is therefore affected 'with a public interest', within the meaning of the doctrine which Lord Hale has so forcibly stated. But we need not go further. Enough has already been said to show that when private property is devoted to a public use, it is subject to public regulation. This brings us to inquire as to the principles upon which this power of regulation rests in order that we may determine what is within and what is without its operative effect. Looking then to the common law, whence comes the right which the Constitution protects, we find that when private property is affected with a public interest it ceases to be *juris privati* (of private right) only."

The question at issue in the Munn case was in respect

[1] 94 U. S. 77.

to the power of the State to fix maximum rates of storage to be charged by grain elevators, and because the business so carried on affected, as the court held, the public interest, it was subject to a greater extent to the regulative powers of the State. Familiar illustrations of quasi-public corporations are: common carriers, gas, telegraph, telephone, elevator, and express companies.

This power of regulation is generally exercised by the State through administrative boards or commissions created by law and limited strictly in the exercise of their powers to those granted directly or specifically by statute. The Federal Government exercises its supervisory powers over common carriers engaged in the business of conducting interstate commerce through the Interstate Commerce Commission.

When the doctrine of regulation was definitely and authoritatively established by the decision in the Munn case, the popular idea of the effect of the decision was that the power to regulate could be exercised by the State without restraint. The Supreme Court of the United States, in the next case[2] before it involving the same question, hastened to hold that the power of regulation was not an equivalent of the right of confiscation and that the State could not in the exercise of the power possessed deprive private corporations of their property without due process of law, or appropriate their property without the payment of just compensation. The court, in its opinion by Chief Justice Waite, said:

"From what has thus been said, it is not to be inferred that this power of limitation or regulation is itself without limit. This power to regulate is not a power to destroy, and limitation is not the equivalent of confiscation. Under pretense of regulating fares and freights, the State cannot require a railroad corporation to carry persons or property without reward; neither can it do that which in law amounts to a taking of private property for public use without just compensation or without due process of law."

[2] Stone *et al.* v. Farmers' Loan & Trust Co. 116 U. S. 307.

The modified doctrine of the Munn case, as thus stated in the Stone case, has been repeatedly followed by the Supreme Court of the United States, and is the established doctrine, therefore, relating to the exercise of the power of regulation of quasi-public corporations by the State. The power to regulate is not synonymous with a power to destroy or to confiscate, but must be exercised within constitutional provisions not contrary to constitutional prohibitions, and must be of a reasonable character.

§ 25. Power of Regulation Further Considered. The power of regulation, as stated in the preceding section, and in respect to quasi-public corporations, is based upon the distinction between a public employment and a private business, and depends upon the fundamental duty of the State to protect the public and to prevent extortion and discrimination in the supply of the necessaries of life, whether these are articles consumed or services rendered. Whether a business is public or private seems to depend upon whether it is a monopoly or not. The distinction between a public employment and a private business is an old one, and in respect to public employments there has been a persistence of State regulation for many years. Necessarily, with changed commercial and social conditions employments considered public many years ago have ceased to be regarded in this light, and others formerly considered as private in their nature are now held to be public employments. The grant of legal privileges is not necessarily a ground for regulation. The right of eminent domain given by the State to certain quasi-public corporations does not make them such, but this right is granted by the State because of the nature of their business as a public employment. The authorities are fairly well agreed that virtual monopoly is the only basis of regulation, and this may exist either by or through the grant of exclusive privileges or franchises, so-called; through the character of the business conducted or carried on by the corporation; through the existence of an established plant the duplication of which by other corporations could only be accom-

plished by the expenditure of large or prohibitory sums of money; through the exclusive ownership of natural products, a limited supply of which exists; or through the ownership of natural locations especially adapted for the rendition of the service or the manufacture of a particular commodity.

§ 26. The Objects of Regulation. The courts are agreed that the two chief objects of the regulation of quasi-public corporations are: first to prevent extortion and to secure a reasonable charge for the service rendered or the commodity supplied; and, second, to prevent discrimination or the giving of undue preferences either as between persons and localities or in service.

From the standpoint of the quasi-public corporation which, it will be remembered, is a private one, the process of regulation cannot go to the extent of fixing a charge for its services so low that no return or an unreasonably low return will be had upon the private property invested in the enterprise. If this is done, it will amount to a taking of the property without due process of law; or a confiscation of property without the payment of just compensation; and these results are prevented through the application of constitutional provisions. The courts have held that the rendition of services, transportation by common carriers, for illustration, is property, and that the State cannot fix, in the exercise of its regulative powers, so low a price to be paid by the public as to compel it to carry on its business at a loss, or otherwise than as indicated in the following paragraph. This, they say, would be a confiscation of private property or a taking of private property belonging to a private corporation without due process of law.

In general, therefore, the courts, without exception, have sustained the doctrine that the rendition of a service, whether that of transportation or the supplying of some commodity, is property within the meaning of constitutional provisions relative to the taking of property without due process of law, or without the payment of full and

ample compensation when it is private, as in the case of all quasi-public corporations, for a public use. The rates charged by water and gas companies, telegraph, telephone, common-carriers and others of a similar character, while they cannot be exorbitant, unreasonable, or discriminatory, must be such as to afford the private property employed in such an enterprise a fair return upon the investment, taking into consideration the character of the service rendered, the nature and risks of the particular business and the return afforded upon the investment of private capital.

§ 27. The Charter of a Corporation: Its Legal Nature. The charter of the corporation is the source of its powers, and it has been held to include not only the popular concept of a charter, viz., the articles of incorporation, but, in addition, constitutional provisions and general laws affecting the particular corporation under consideration and decisions of the highest courts construing, interpreting or applying phrases and words to be found in any of the three things noted.

It is regarded, in its legal nature, as a contract[3] which may be defined as an agreement upon a sufficient consideration to do or not to do a particular thing, and the essentials are mutuality or a meeting of the minds in respect to the object or subject of the contract and a consideration. As a contract, it has been held that it comes within that provision of the Federal Constitution prohibiting a State from passing any law impairing the obligation of a contract. The parties to this contract are the State and the corporation; the State and the members of the corporation; the corporation and its members; and in some instances the creditors of the corporation have been regarded as parties to the contract relation.

§ 28. The Charter as a Contract. The several contractual relations enumerated in the preceding section can be somewhat amplified:

First, the charter as a contract between the State and

[3] Trustees of Dartmouth College v. Woodward, 4 Wheaton (U. S.) 516.

the corporation. It is evident that the grant of corporate rights may contain valuable privileges of which the corporation cannot be deprived by the State under the contract theory. The right to conduct a certain business; a prescribed period of time during which this can be done; the manner or the place in which the corporate business can be transacted; in fact, nearly all of the powers of the corporation as contained in the charter constitute valuable privileges and form a part of the contract which exists between the State and the corporation.

Second. The charter as a contract between the State and the stockholders. The right to charge a certain rate of interest upon loans as granted by a corporate charter; a particular method provided for the election of directors by the stockholders; their power to elect directors by cumulative voting, and certain prescribed rights of the minority in respect to the management of the corporation are illustrations of charter provisions which may constitute contract rights.

Third. The charter as a contract between the stockholders. The contractual nature of the relation between the stockholders is so plain as to require no more than its mere suggestion. The members are bound by charter provisions in respect to internal management or control. Through the operation of this principle, the majority of the members cannot adopt a by-law which is in contravention of the terms of the charter of the corporation; and it has also been held that as an essential part of the contract rights between the members, it operates to prevent the majority from so controlling or exercising the corporate powers as to pervert or destroy the original purposes of the corporation.

§ 29. The Consideration. The consideration moving from the State to the incorporators is the privilege or right of being incorporated and acting in a corporate capacity, exercising corporate powers. The consideration moving from the incorporators to the State, as said by Justice Story in the Dartmouth College case, is the benefit and

advantage derived by the State or the public at large from the organization of the corporation and the resulting prosperity of the community. Chief Justice Marshall also said, in the same case, that the objects for which a corporation is created are universally such as a government wishes to promote. They are deemed beneficial to the country, and this benefit constitutes the consideration, and in some cases the sole consideration of the grant. In those States where substantial fees are charged for the organization of corporations, it has been suggested that the payment of these fees by the incorporators, in addition to the general benefits and advantages noted above, is to be regarded as a part of the consideration for the grant by the State to them.

§ 30. The Dartmouth College Case. The importance of the Dartmouth College case and its consequent result upon the law of private corporations in this country justifies some further reference to it. The charter of Dartmouth College, as originally granted by the British Crown prior to the Revolution, limited the number of trustees to twelve, conferred upon them the full power of governing the college, including the right of filling vacancies occurring in their own body, and of appointing and removing instructors. After the Revolution, the legislature of New Hampshire passed a law to amend the charter and to improve and enlarge the corporation. It increased the number of trustees to twenty-one, gave the appointment of the additional members to the executive of the State, and created a board of overseers to consist of twenty-five persons, of whom twenty-one were also to be appointed by the executive. These overseers had power to inspect and control the most important acts of the trustees. An action of *trover* was brought by the trustees of the Dartmouth College against William H. Woodward in the State courts of New Hampshire to recover the book of records, corporate seal and other corporate property to which the plaintiffs alleged themselves to be entitled. A special verdict was found for the defendant if certain acts of the legislature

of New Hampshire, those already referred to, were valid and binding on the trustees without their assent, and at the same time were not repugnant to the Constitution of the United States; otherwise the verdict was to be found for the plaintiff.

The Superior Court of Judicature of New Hampshire rendered a judgment upon this verdict for the defendant, which judgment was brought before the Supreme Court of the United States on writ of error, and the single question considered by that court was whether the acts to which the verdict referred violated the Constitution of the United States. The contention of the trustees was that the original charter or grant constituted a contract as between the sovereign State and the corporation, the obligation of which could not be impaired by subsequent legislation on the part of the State, invoking, in support of their contention, that provision of the Federal Constitution which prohibits a State from passing any law impairing the obligation of a contract. Chief Justice Marshall wrote the principal opinion and on the main question said, in the course of his decision:

"This is plainly a contract to which the donors, the trustees, and the Crown (to whose rights and obligations New Hampshire succeeds) were the original parties. It is a contract made on a valuable consideration. It is a contract for the security and disposition of property. It is a contract on the faith of which real and personal estate has been conveyed to the corporation. It is a contract then within the letter of the Constitution, and within its spirit also, unless the fact that the property is invested by the donors in trustees for the promotion of religion and education for the benefit of persons who are perpetually changing, though the objects remain the same, shall create a particular exception taking this case out of the prohibition contained in the Constitution. . . . The opinion of the court, after mature deliberation, is that this (referring to the charter) is a contract, the obligation of which cannot be impaired without violating the Constitution of the United States. This opinion appears to us to be equally supported by reason and by the former decisions of this court."

The decision then proceeded to hold that the acts of the legislature of New Hampshire constituted an impairment of the contract obligation of the charter and were, therefore, unconstitutional as contravening the constitutional provision above referred to. Justice Miller referred[3] to this decision in the following language:

"It may be well doubted whether any decision ever delivered by any court has had such a pervading operation and influence in controlling legislation as this."

And, again, in speaking of this case, he said:

"The opinion, to which there was but one dissent, establishes the doctrine that the act of a government, whether it be by a charter of the legislature or of the Crown which creates a corporation, is a contract between the State and the corporation, and that all the essential franchises, powers and benefits conferred upon the corporation by the charter become, when accepted by it, contracts within the meaning of the clause of the Constitution referred to."

The practical effect of this decision is to restrict the power of the State in the passage of legislation, altering, amending or repealing existing laws under which corporations have become incorporated and under authority of which they are exercising the powers, privileges or capacities already granted. Or, to state the principle differently, the charter of the corporation, for example, the source of its powers, can not be subsequently changed or repealed by the State without the consent of the corporation and the other parties to the contract contained in it.

The far-reaching effect of this decision was clearly perceived by the court, for Justice Story, in a concurring opinion, suggested that if the legal effect of their decision should be deemed against public policy, that it would be a comparatively easy matter for subsequent legislative acts granting corporate rights and charters to reserve expressly to the State the power to amend, alter, or repeal them. The doctrine of the Dartmouth College case has been widely

[3] Lectures on the Constitution, 392.

criticized, but on reflection and on examination of the inherent and reserved powers of the State, it will be seen that it is correct in principle, and that as to all of the essentials of regulation and control the powers of the State are not diminished.

§ 31. Meaning of the Word Law. The word law is used in the Federal Constitution in the prohibition relating to the impairment of the obligation of contract rights, and controversy arose later in respect to its exact significance. By a series of decisions the accurate meaning of the word law as thus used is now held to include not only the acts of any lawmaking body of the State, constitutional provisions or amendments, but also decrees or judgments of a court of last resort in a State to which it gives the force and effect of a law. In other words, the term law is held to include any act of the State to which it gives the force and effect of a law.

§ 32. Inherent Power of the State to Regulate through Its Police Power. Let us consider, first, some of the inherent and inextinguishable rights of a State to control and regulate the acts of all persons and the use of property within its jurisdiction even though their exercise may affect the powers or the capacities of corporations already in existence and exercising them under previous authority from the State. The most important of these is termed the police power. This cannot be relinquished even by the express provisions of a charter so as to defeat the right of the legislature to subsequently act in respect to it, much less to operate as a restraint upon future legislative bodies. Judge Cooley declared:[4]

"That all contracts and all rights are subject to this power. And not only may regulations which affect them be established by the State, but all such regulations must be subject to change from time to time as the general well-being of the community may require or as the circumstances may change or as experience may demonstrate the necessity."

[4] Cooley, Constitutional Limitations (7th ed.) p. 833.

Definitions, or attempted definitions, have been given in many cases and by many legal authors. As an example:

"This police power of the State extends to the protection of the lives, limbs, health, comfort, and quiet of all persons, and the protection of all property within the state."[5]

All agree, however, that this power of the State extends to the protection of its peace, good order, good morals, welfare, and the health, lives, and limbs of its people, and in the absence of constitutional provisions limiting the manner of its exercise, a lawmaking body may prevent all things hurtful to the safety, the welfare, and the comfort of society, even though such legislation invades the right of liberty or affects the property of individuals. This power is inherent, inextinguishable, continuing and not subject to surrender or barter.

§ 33. Restrictions upon an Exercise of the Police Power. Limitations upon the exercise of the power necessarily exist and for the purpose of this work two of the more important only will be suggested. These are, that the subject of an attempted exercise of the police power by the State must have some relation to the nature of the power; that is, some reference to the peace, health, safety, and good order or the good morals of the community; and also that the regulations adopted by a State, or any of its subordinates, in the ostensible exercise of the power must be reasonable and necessary. As said by one court:

"It is not within the power of the general assembly, under the pretense of exercising the police powers of the State to enact laws not necessary to the preservation of the life and safety of the community that will be oppressive and burdensome upon the citizens. If it should prohibit that which is harmless in itself, or command that to be done which does not tend to promote the health, safety, or welfare of society, it would be an unauthorized exercise

[5] Thorpe v. Rutland, etc., R. R. Co. 27 Vt. 140.

of the power and it would be the duty of the courts to declare such legislation void."[6]

In the valid exercise of the police power, therefore, the conduct of the business of a corporation, or the business itself, or the exercise of corporate powers theretofore legally granted, may be regulated and controlled by the State, though its action in this respect tends to lessen the corporate capacity, or, in some cases, to prevent it entirely from carrying on or conducting its business.

Police Power; Discussion and Illustration of Its Exercise. The existence of dual sovereignties in the United States and the fact that to the Federal Government is given certain exclusive powers, operate as a restriction upon an exercise by the States of the police power in respect to corporations. The power of the Federal Congress to pass laws regulating interstate commerce, for example, is exclusive in that body, and the several States cannot act where an attempted exercise of the police power is in effect, a regulation of interstate commerce. The States, however, possess certain exclusive powers, and there are also others which may be concurrently exercised by both the Federal Congress and the States, and the right in each sovereignty, therefore, remains unrestricted except as controlled by constitutional provisions. Corporations, equally with other persons, are subject to the proper exercise of the police power of both the Federal Government and that of the States, and this has been exercised in many cases in such a way as to diminish corporate rights previously granted or to affect the manner in which corporate business has previously been transacted, acts which, if not done under the police power, would amount to an impairment of charter privileges and, therefore, contract rights. Legislation has been passed in many instances establishing limitations upon the power of making contracts between the corporation as an employer and its employes; provisions fixing hours of labor, and especially those for women and chil-

[6] Toledo, etc., R. R. Co. v. Jacksonville, 67 Ill. 37.

dren; requirements in respect to the filing of reports by corporations; inspection laws affecting, in many cases, the carrying on of the business of the corporation for which it was directly authorized by its charter; regulations governing the importation or transportation of diseased animals; and provisions regulating the manner in which the business of common carriers is to be conducted. The latter acts have for their especial purpose the protection and safety of travelers and other persons either employed by the corporation or those whose safety will be enhanced by reason of the regulations. The adoption of laws or municipal ordinances controlling the speed of trains in cities or at crossings or providing for the erection of safety gates; tests for color blindness for engineers, are familiar examples; and many others of a similar nature will suggest themselves to the reader. The police power of the State also extends to the control and regulation of rates for services or commodities furnished by quasi-public corporations, but this subject has been sufficiently discussed in a preceding section. Proper police regulations may even extend to the abolition of a business or occupation previously carried on by a corporation under authority of law. This principle is well illustrated in the cases of Stone v. Mississippi, and Beer Company v. Massachusetts.[7] In the former case the court said:

"No legislature can bargain away the public health or the public morals. The people themselves cannot do it, much less their servants. The supervision of both these subjects of governmental power is continuing in its nature, and they are to be dealt with as the special exigencies of the moment require. Government is organized with a view to their preservation and cannot divest itself of the power to provide for them. For this purpose the largest legislative discretion is allowed, and the discretion cannot be parted with any more than the power itself."

In the latter case certain malt liquors belonging to the Boston Beer company had been seized as it was transport-

[7] 101, U. S. 814; 97, U. S. 25.

ing them to its place of business with the intent there to sell them in violation of a prohibitory liquor[8] law passed subsequent to the organization of the corporation, which was created for the especial purpose of engaging in the manufacture and sale of malt liquors. The company claimed that under its charter it had the right to manufacture and sell said liquors and that the prohibitory law impaired the obligation of the contract contained in that charter and was void so far as its business and property was concerned. In passing judgment upon this point, the court said:

"The plaintiff in error was incorporated 'for the purpose of manufacturing malt liquors in all their varieties,' it is true; and the right to manufacture, undoubtedly, as the plaintiff's counsel contends, included the incidental right to dispose of the liquors manufactured. But although this right or capacity was thus granted in the most unqualified form, it cannot be construed as conferring any greater or more sacred right than any citizen had to manufacture malt liquors; nor, as exempting the corporation from any control therein to which a citizen would be subject, if the interests of the community should require it. If the public safety or the public morals require the discontinuance of any manufacture or traffic, the hand of the legislature cannot be stayed from providing for its discontinuance by any incidental inconvenience which individuals or corporations may suffer. All rights are held subject to the police power of the State. We do not mean to say that property actually in existence, and in which the right of the owner has become vested, may be taken for the public good without due compensation, but we infer that the liquor in this case was not in existence when the liquor law of Massachusetts was passed. . . . The plaintiff in error boldly takes the ground that being a corporation it has a right by contract to manufacture and sell beer forever, notwithstanding and in spite of any exigencies which may occur in the morals or the health of the community, requiring such manufacture to cease. We do not so understand the rights of the plaintiff. The legislature had no power to confer any such rights."

[8] 97, U. S. 25.

This same idea is also expressed in the Stone case previously cited, where the court said that in passing upon the question of whether a law had been passed impairing the obligation of a contract, the first query of the court would be to ascertain whether any contract existed and it was then held that the State could make no contracts surrendering or limiting its right at any time to exercise its police power.

§ 34. **Eminent Domain.** The inherent continuing and inextinguishable power of eminent domain possessed by all sovereignties also in its exercise may operate as a regulation or control of corporations despite the contract doctrine of the Dartmouth College case. This power is one which gives to the State or its delegated agencies the right to appropriate or take private property for a public use upon the payment of just compensation. The courts hold, however, that the compensation secured by constitutional provisions providing for the exercise of the power must be full, ample, just and complete. The property of corporations, equally with that of natural persons, is subject to the exercise of this power, and it has been suggested in some cases that even the franchises of the corporation may be taken for a public use upon the payment of just compensation.

§ 35. **Taxation.** The power of the State to compel the payment of an equivalent contribution from persons and property within its jurisdiction for its support is also one of the continuing, inherent and inextinguishable prerogatives or powers of sovereignty, and unless there exists a valid exemption as to corporations or their property from taxation, or a limitation upon the amount which can be collected, the state can exercise freely, subject only to constitutional provisions, this power in respect to the properties of private corporations. As a theory, this power is without limitations, but in the United States, the Constitutions both of the United States and of the several States contain provisions which, in effect, limit and restrict its exercise. These limitations apply to the property of pri-

vate corporations equally with that belonging to other persons. A few of the more important may be suggested. In the first place, the power can only be exercised for what is known as a public purpose. The State cannot use its power of taxation for the purpose of taking property from one citizen to be given to another. The use of the moneys obtained by taxation is limited to governmental purposes or objects. A State is also restricted in the exercise of its power of taxation to persons or property within its jurisdiction. This principle is axiomatic. The laws or the powers of the sovereign can extend no farther than its geographical limits. The property, therefore, of a corporation, unless within the jurisdiction of the State, cannot be taxed. The principles of uniformity and equality must also be applied by the State in respect to the taxation of the property of corporations.

It has already been suggested that in this country exist dual sovereignties, the United States of America and the several States. The Federal Constitution gives to the United States certain prohibitive powers over the sovereign acts of the different States. A few may be mentioned: a State cannot pass any law impairing the obligation of a contract. It must give to each citizen the equal protection of its laws. It cannot deprive any person of life, liberty or property without due process of law. Private property cannot be taken for a public use without the payment of just compensation; a State cannot make or enforce any law which shall abridge the privileges or immunities of citizens of the United States. The power of the States over corporations created under the Federal laws is limited in all respects and this is especially true of those corporations organized by the Federal Government as agencies of its own in carrying out or executing some of the powers directly given to it in the Federal Constitution. The banks organized under the National Banking Laws are good illustrations of the latter class of corporations.

§ 36. Reservation of Right to Amend, Alter, or Repeal. It has already been noted that Justice Story, in the Dart-

mouth College case, suggested that the States might, in the passage of laws providing for the creation of corporations, reserve directly the right to amend, alter, or repeal them. The States, without exception, have followed this suggestion. The legal effect of such a reservation is to make the power of the State in respect to amendment, repeal or change, a part of the charter and its resulting contract. Subsequent legislatures, therefore, can change, repeal or alter laws relating to the incorporation and organization of corporations and the conduct of their business without the contention being raised that this action is tantamount to an impairment of the contract obligation and therefore unconstitutional under the well known provision of the Federal constitution.

The possession of this power to amend, alter, or repeal by the State, however, does not give to it, as might be gathered from the phraseology, the unlimited and unrestricted power to deal with corporations and their property. Some well established principles construing the right to amend, alter, or repeal will be noted in the following section.

§ 37. Limitations upon the Reserved Right to Alter, Amend, or Repeal. Where the State has expressly reserved the right to repeal the charter of a corporation at that time granted it, no question can be raised if subsequently the power of repeal is exercised. To expressly reserve the right to repeal, and then to withhold from the legislature the legal right of exercising the power directly reserved would be an absurdity. It can be no breach of a contract to enforce its terms. Where the power to amend is alone given, the courts hold that this is not equivalent to the power of repeal; that a new charter cannot be forced upon a corporation through the power of amendment, nor can an existing charter be taken away; and, further, that the State cannot compel the corporation to do business under an amendment. The power to amend is limited to action in consonance with the general powers and capacities of the corporation as originally created. Where the power to

alter, amend, or repeal has been reserved, the question presents greater difficulties. Thompson on Corporations[9] summarizes the authority and the powers of the State under these circumstances as follows:

"However, in such case the corporation is entitled to some protection. On reason and authority the corporation is entitled to protection as against any amendment or repeal under such reserved right: (a) that would amount to a confiscation of property; (b) that would defeat or substantially impair the object of the original grant; (c) that would force the corporation into enterprises not contemplated by the original charter; (d) that would deprive incorporators of the control of the corporate property; (e) that would authorize a disturbance of vested rights; (f) that would take from the corporation its funds or property without compensation or due process of law; (g) that would annul or dissolve contracts already executed; (h) that would amount to punishment for acts lawful when committed; (i) that would affect or change the rights of the stockholders as among themselves; (j) that would extend to giving a power to one part of the corporators as against the other which they did not have before; (k) that would abridge the lawful rights of the stockholders. These principles are also supported by the leading law-writers."

It must be remembered that in connection with the possession of the power on the part of the State to alter, amend, or repeal, fundamental rights stated in the Constitution of the United States or the constitutions of the different States operate as a limitation. These basic principles, the application of which is extended not only to personal but also to property rights, are designed for the protection of artificial persons or corporations equally with individuals. At the present time, when the inclination exists, even on the part of well meaning executive officials of high station as well as members of legislative bodies, to forget or ignore the paramount and organic law, viz, our constitutions, it might be well to call attention to some provisions having for their purpose the objects above sug-

[9] Thompson on Corporations, 2d ed., § 341.

gested. No person, including a private corporation, shall be deprived of life, liberty, or property without due process of law; nor shall private property be taken for public use without just compensation. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States, nor shall any State deprive any person of life, liberty, or property without due process of law, nor deny to any person within its jurisdiction the equal protection of the laws. Under these provisions, as well as others, the courts have decided that even where the power is reserved to alter, amend, or repeal the charters of private corporations a State cannot so legislate as to destroy or impair contract rights, either of the corporation or of its members, previously acquired in the lawful exercise of its corporate powers. That they cannot so legislate as to effect an injustice to the members of a corporation; that the contractual rights of members, as among themselves, cannot be destroyed or impaired, and that under all circumstances and on all occasions no action can be taken by the State which will destroy or lose to the corporation and its members the property of the corporation. Amendments to the charter cannot be forced upon a corporation. This principle obtains because the organization of a private corporation is the result of purely voluntary action on the part of its members. The State cannot compel a group of persons to organize and conduct a private business enterprise under a corporate form. It is within the privileges of a corporation, where a radical amendment has been passed, to wind up its affairs. Rights acquired by the corporation and which are not included within the contract terms of the grant cannot be made the subject of amendatory legislation. "Personal and real property acquired by the corporation during its lawful existence, rights of contract or choses in action so acquired and which do not in their nature depend upon the general powers conferred by the charter, are not destroyed by such a repeal." [10]

[10] Greenwood v. Freight Company, 105 U. S. 13.

The Supreme Court of the United States, in another case,[11] held:

"All agree that it cannot be used (referring to the power to alter, amend, or repeal) to take away property already acquired under the operation of the charter or to deprive the corporation of the fruits actually reduced to possession of contracts lawfully made."

And again this court said, in another case:

"The power reserved to the legislature to alter, amend, or repeal a charter authorizes it to make any alteration or amendment of a charter granted subject to it which will not defeat or substantially impair the object of the grant or any rights vested under it and which the legislature may deem necessary to secure either that object or any public right."

The term law as used in the contract obligation clause of the Federal Constitution has already been defined as including the act of any law-making body of a State. Municipal corporations are frequently created by State authority and a portion of its legislative power delegated to subordinate legislative bodies known as municipal councils, or some equivalent term. The protection of the Federal Constitution applies to the legislative acts of these subordinate law-making bodies equally with the action of a State legislature, and the principles in respect to the protection of property and vested rights, briefly stated in this and the preceding paragraph, also refer to the legislative acts of municipalities.

§ 38. The Charter of a Corporation: Its Construction. The charter of a corporation is the source of its powers; the fountain of its legal authority to act in its corporate capacity. The charter, as will be remembered, includes not only the articles of incorporation, as executed by the incorporators, but also general laws and constitutional provisions referring to the particular class or kind of corporation. Owing to the diverse character and qualifications of

[11] Union Pacific R. R. Co. v. United States, 99 U. S. 700.

the members of the legislative bodies, it is natural that at times, language ambiguous and indefinite in its character may be found in grants to corporations, or laws under which they may be created and corporate powers exercised. The occasion, therefore, frequently arises for a construction and interpretation of the charter of the corporation. Rights and privileges may be claimed and their existence denied. It is then the duty of the courts to pass upon conflicting claims. What rules of interpretation are adopted by them in the determination of these issues? It might be said that generally the courts, where the question is raised of the meaning of a word or phrase, the existence of alleged conditions or the application of particular laws, follow either the rule of strict or of liberal interpretation or construction. Where the former is adopted, the existence of the right or the application of the law is decided in favor of the doubt. If the rule of strict interpretation is adhered to, the doubt is resolved against the existence of the right or condition or the application of the law.

The organization of corporations and the conduct of their business is not only made legal by the State but is encouraged as a matter of public policy because of the resulting benefit and advantage to the community. The grant of corporate power may be either the authorization to transact a business or to carry on an occupation under corporate form which natural persons as a matter of common right could engage in or carry on. On the other hand, powers or capacities may be granted to a private corporation which are exclusive in their character,[12] or exemptions and special privileges may be granted to them to possess and to enjoy which the citizens of the country, as a matter of common right, are not entitled to possess or enjoy. Stating the proposition more concisely, corporations may enjoy and possess either rights of an ordinary and natural character, or special privileges and exemptions not existing as a matter of common right, nor without a special grant of the State. Because of the favorable attitude of the State to-

[12] Close v. Glenwood Cemetery, 107 U. S. 466.

wards corporations, the courts generally adopt, in the interpretation of a charter, the liberal rule in respect to the exercise of all the ordinary and usual powers of the corporation. That rule of construction is also followed which tends to facilitate the carrying on of the corporate business and the success of the enterprise, if there is not involved a doubt as to the existence of a special privilege or exemption. The rule of strict construction, on the other hand, is universally applied in connection with the exercise of exclusive privileges, franchises, and exemptions. Where a grant to a corporation is made in derogation of the common right, as the phrase is sometimes stated, if any doubt exists as to its existence, or the extent of its application, or the manner in which it can be exercised, that doubt is resolved most strongly against the corporation and in favor of the State.

Since the charter of a corporation consists largely of the acts of law-making bodies, the rules or canons of construction usually applying to legislative acts will also be applied to that legislation referring to and affecting private corporations. One canon or rule of construction is that the intent of the legislature is to be ascertained if possible in cases of doubt as to the meaning of words or phrases or the existence of a right. General words, followed by specific enumeration, are limited in their meaning to the rights or powers conveyed or included in the words of narrower or restricted meaning. The doctrine of exclusion, so-called, is also frequently applied and followed by the courts in determining the extent of corporate powers.

§ 39. Construction of Charters: Strict and Liberal Rules. From an examination of the authorities it will be easily ascertained that corporations exercise, under their charters, two classes or kinds of corporate power, viz, those which might be termed as the usual and ordinary acts essential to the transaction of their business as corporations and others involving the exercise of the rights granted by the State of an extraordinary or exclusive nature. The liberal rule is undoubtedly adopted by the courts in construing and applying the former, while, with-

out exception, the strict rule is followed in determining corporate rights of the latter class. Phrases and decisions are constantly found to the effect that the charter of a corporation is to be strictly construed as against it and in favor of the public; that nothing can pass by implication and that no corporate capacities can be exercised unless they are clearly and unequivocally expressed. Upon examination of the cases, it will be found that these principles, in their severity, apply to special privileges, powers, or exemptions claimed by the corporation. There will be found also decisions holding that the strict rule of construction applies to all the powers or capacities claimed by the corporation, but the weight of authority as gathered from the more recent decisions without doubt holds along the lines suggested. This modern rule is, clearly, the correct one, and is well stated in Thompson on Corporations:[13]

"Ordinarily the interpretation is not to be opposed to the general purposes of the grant, except where the restrictive language of the charter itself is such that it cannot be overlooked or disregarded. On this theory of interpretation, statutes, and charters are permitted to include devices, instrumentalities and methods of conducting business unknown and not in use at the time of the adoption of such charter. This rule of progressive construction permits corporations to keep pace with the progress made in inventions and appliances, and extends jurisdiction to protect plans and methods of transacting business which were not known and could not have been stated in the charter at the time it was granted."

In a Pennsylvania case it was stated:[14]

"It is doubtless true that such charters are to be construed most beneficially for the public and most strictly against the company, but the construction must be a reasonable one. The charters of most private corporations are for purposes of private gain, and many of them grant exclusive privileges in abridgement of individual rights,

[13] Thompson on Corporations, 2d ed., § 309.

[14] Brown v. Susquehanna Boom Co. 109 Pa. St. 57.

but as they are intended to subserve public interests they should be so construed as not to defeat the purpose of their creation. . . . Whilst, therefore, the words of the charter should be construed with some degree of strictness for public protection, it should not be construed to require the performance of what, in the nature of the case, cannot be performed."

The liberal rule of construction, it will be found also, upon an examination of the cases, to be applied with less frequency in the case of quasi-public corporations. This principle further illustrates the distinction attempted to be made above in the nature or character of the powers exercised by the corporation. The liberal rule is also used where the corporation is seeking to avoid a liability through a strict or technical construction of its charter. The subject of the construction of the charter is so intimately connected with the exercise of its powers that a further discussion will be had of the principles followed in the chapter on corporate powers. Thompson on Corporations[15] states as a few fundamental rules, which apply to the interpretation of charters, the following:

"(a) Charters are to be construed as contracts between the government and the corporation and not as mere laws; (b) Charters are to receive a reasonable construction, and if the intent can be satisfactorily made out from the express words, and from the just and plain inference from the terms used, it is to prevail and to be carried into effect; (c) If the language of the charter be ambiguous, or the intent cannot be satisfactorily made out from the terms used, then it is to be taken most strongly against the corporation and most beneficially to the public; (d) A right not given in express words by the charter may be deduced by interpretation, if it is clearly inferable from some of its provisions."

And another rule was given by Lord Coke:[16]

"The best exposition of the king's charter is, upon the consideration of whole charter, to expound the charter by

[15] Thompson on Corporations, 2d ed., § 297.

[16] Sutton Hospital Case, 10 Coke 1.

the charter itself, every material part thereof being explained according to the true and genuine sense, which is the best method."

§ 40. Franchises and Privileges. In a more extended work this subject would receive extended and separate treatment. In this elementary treatise, a discussion naturally falls under the chapter on the State and the corporation, and must necessarily be limited to a few sections. It will be somewhat difficult to state in the space assigned in a concise and strictly accurate manner the essential questions involved. This difficulty arises both from the nature of the subject and also from the different conceptions of it by judges and lawmakers. The definition most frequently given of a franchise is that of Chief Justice Taney in a case in 1839,[17] where he defines franchises as

"Special privileges conferred by government upon individuals and which do not belong to the citizens of the country generally of common right. It is essential to the character of the franchise that it should be a grant from the sovereign authority, and in this country no franchise can be held which is not derived from the law of the state."

The authorities are generally agreed that the term can be used in a primary and secondary sense. The right of an incorporated company "to be a corporation, or the right conferred upon it by the State to be an artificial body, has been called its primary franchise, and this has been distinguished from what is termed its secondary franchises which include the right to carry on or transact a particular kind of business as in the case of the privileges granted to a water company with the right to take tolls, etc., or the right of a railroad to collect fares or of a toll road company to exact toll for services performed."[18]

This distinction is an essential one to bear in mind in connection with the right of the State to regulate or control the corporation, to amend, alter, or repeal its char-

[17] Bank of Augusta v. Earle, 13 Peters (U. S.) 519.

[18] Joyce on Franchises § 8.

ter, or to determine the extent of the capacities enjoyed by a particular corporation. A clear distinction exists between the grants of franchises which are essential to the creation and the continued existence of the corporation, to its right as a distinct legal entity, and other privileges or powers given to it that are not essential or prerequisite to its corporate existence. The purposes of corporate existence are quite distinct from the franchises of the corporation. A franchise to be a corporation is distinct from a franchise as a corporation to maintain and operate a railway.

In the Chicago City Railways[19] case, the Supreme Court of the United States held that the franchise of existing as a corporation was given by the State and was distinct and separate from the privilege or license given by the city of Chicago to the corporation to operate and maintain a system of street railways upon its highways. In another case,[20] this distinction is also emphasized:

"This corporate franchise, viz, the franchise to be and exist as a corporation for the purposes specified in the articles of incorporation, appertains to every corporation, for whatever purpose it may be formed, and there is no distinction in this regard between the banking or grocery corporation, and the railroad, water, or gas corporation. The right to engage in every such business is open to all citizens, independent of any grant from the sovereign, but it is available to no one to conduct any such business through the agency of a corporation without such grant. Certain occupations are, however, of such a nature that various privileges conferable only by the sovereign power are convenient, and in most cases absolutely essential, to the successful maintenance of the business to be carried on, whether it be carried on by a corporation or by an individual, such, for instance, as the right to use public highways. Such rights and privileges are also known as franchises, but they constitute a class entirely distinct from and independent of the corporate franchise."

The distinction is practically applied where the existence of the power to exercise certain rights is at issue.

[19] Blair v. Chicago, 201 U. S. 400-460, 50 Law ed. 801.

[20] Bank of California v. San Francisco, 142 Calif. 276.

Where franchises, as the word is used in its secondary sense, are claimed, the rule of strict construction undoubtedly exists; while the liberal rule would be followed in respect to the exercise of franchises which belong to the first class, or where the word is used in its primary sense.

§ 41. **Exclusive Franchises.** All franchises granted may be of an exclusive character or otherwise. The word exclusive as used in this connection is self-definitive. The right or privilege to exist as a corporation for a specified purpose, or of exercising certain corporate capacities or powers is given by the State to a group of persons to be exclusively exercised or possessed by them in a corporate capacity. An exclusive grant of this character is regarded as a contract, and if the State attempts to give to other persons the same or equivalent rights this act will be regarded as an impairment of the contract obligation. On the other hand, if certain corporate rights and capacities are granted with no words expressly stating their character as exclusive, the State, undoubtedly, is not limited in its power to grant to other corporations like privilege and capacities.

§ 42. **Nature of Franchise.** A franchise, whether the word is used in its primary or secondary sense, is usually regarded as a contract right, controlled by the principles already stated. The permission of the State or of a subordinate agency, viz; a municipal corporation, to exercise a corporate power or to conduct a business, the legal authority to do which has been already granted by the State, is considered by the courts usually as a mere license or the grant of a privilege which may or may not be legally regarded as a contract. Its nature in this respect will be determined by the language of the grant. The license may be merely a revocable privilege. There are many illustrations of franchises, privileges, or licenses granted to corporations in modern times. The right to exercise the power of eminent domain by railroad corporations; to establish ferries or bridges; to construct and maintain systems of street railways within the limits of municipalities; to establish and maintain plants for the manufacture or supply

of water, light, or power. The right of the State or of the municipality as a subordinate agency of the State to repeal or to alter the terms of the franchise, privilege, or license given, as already suggested, will depend entirely upon the language of the original grant, and whether, under the rule of strict construction, it will be held a contract or merely a revocable license.

§ 43. **Assignability.** Whether a franchise or license granted by State or other lawful authority to a corporation can be assigned and transferred by it to some other group of persons depends largely upon the existence of two conditions. First, can this be done under the language of the grant? In cases of doubt, the rule of strict construction applies. Second, what is the nature of the business to be carried on under the franchise or privilege granted. If it is that usually conducted or carried on by what are known as quasi-public corporations, unless the right to sell, transfer, or assign clearly appears in express terms, it will be denied. This principle of law is based upon the reason that in the grant of these powers to particular corporations a certain degree of confidence is reposed in them in respect to the performance of not only their powers and corporate capacities, but also their duties to the public or community at large. Quasi-public corporations, it will be remembered, are private corporations, but engaged in a business which affects the welfare of the public at large. The State, in the grant of a franchise or privilege to a quasi-public corporation, may consider it inadvisable or against public policy that the rights conferred should be sold or assigned to others lest the full and proper performance of their duties and obligations to the public be impaired or destroyed. A familiar illustration of this principle is to be found in many statutory provisions that prohibit the sale, transfer, or mortgaging of the franchises (using the word in its secondary sense) of a common carrier.

The sale or transfer of the property of a railroad company, which also may be effected through the mortgaging of its franchises, might result in the destruction of bene-

ficial competition existing between several common carriers. The properties and franchises, if a sale or transfer were permitted, might be acquired by one railroad corporation and others, the charters of which had been granted for the purpose of protecting the public against extortion or discrimination, absorbed. The power to sell, transfer, or assign franchises or privileges must be expressly given.

§ 44. Constitutional Protection of Franchises or Privileges. Franchises or privileges, when granted by the State or under its authority constituting a contract as between the grantor and the corporation, will be protected by that clause of the Federal Constitution in respect to the impairment of contract obligations. Constitutional protection will depend entirely upon the language of the grant or franchise. If the privileges are construed as being merely revocable, clearly no contract relation will exist.

CHAPTER VI

TAXATION OF CORPORATIONS

§ 45. Definition and Nature of the Power. It was stated in a preceding section that in the absence of an express exemption, the property of a corporation was subject to the taxing power of the State as one of its inherent and sovereign attributes. The exercise of the power, unless as above stated specifically withheld, does not constitute an impairment of any charter or contract obligation by the State. The power to tax can be exercised both as a regulative measure and also as a source of revenue to the State. The power has been defined as that inherent and continuing power of a State to compel the payment from persons and upon property within its jurisdiction of an involuntary contribution for the maintenance of its organized government. Another definition given by the Supreme Court of the United States[1] is to the effect "that taxes are burdens or charges imposed by the legislative power upon persons or property to raise money for public purposes. The power to tax rests upon necessity as inherent in every sovereignty. The legislature of every free State will possess it under the general grant of legislative power, whether particularly specified in the Constitution among the powers to be exercised by it or not."

And Judge Cooley, in his work on Constitutional Limitations, states both a definition and some inherent limitations upon an exercise of the power in the following language:

"While taxation is in general necessary for the support of government, it is not part of the government itself. Government was not organized for the purpose of taxation, but taxation may be necessary for the purposes of government.

[1] Ashley v. Ryan, 153 U. S. 436.

As such, taxation becomes an incident to the exercise of the legitimate functions of government but nothing more. No government dependent upon taxation for support can bargain away its whole power of taxation, for that would be, substantially, abdication. All that has been determined thus far is that for a consideration it may, in the exercise of a reasonable discretion and for the public good, surrender a part of its powers in this particular."

§ 46. Corporate Property Subject to Taxation. In the case of Tennessee v. Whiteworth,[2] it was held by the Supreme Court of the United States, Chief Justice Waite writing the opinion, that

"In corporations four elements of taxable value are sometimes found: (1) franchises; (2) capital stock in the hands of the corporation; (3) corporate property; (4) shares of the capital stock in the hands of the individual stockholders. Each of these is recognized as an element of a taxable value in a corporation that, subject to constitutional restrictions, can be taxed by the State."

The franchises of the corporation, it has been held in many States, are subject to a separate tax in addition to one on its property of a tangible value or the capital stock of the corporation in the hands of the stockholders or considered as the capital stock of the corporation. The franchises subject to taxation may be the rights and privileges included within the meaning of that word, used either in its primary or secondary sense, the primary meaning being, as previously stated, the right of being a corporation and the exercise of certain ordinary privileges in connection with its existence in a corporate capacity; and, in a secondary sense, the grant of special privileges and exemptions or extraordinary powers not possessed by the people as a matter of common right, or, in some cases, in derogation of common right.

The right of the State to tax the tangible property of a corporation obtains as a matter of course, the only limita-

[2] 117, U. S. 129.

tions being those contained in its own Constitution or that of the United States and which will be noted in a succeeding section. Some States have held that the capital stock of a corporation considered as capital stock is subject to taxation independently of the right to levy a tax upon the other elements of taxable value found in a corporation, or upon its stock considered as the personal property of the corporate stockholders.

Shares of stock in the hands of their owners are considered personal property, and as such subject to taxation by the State. A tax upon shares of stock of the corporation may be effected either through an assessment of the property in the hands of the shareholders, or the corporation itself may be compelled to pay the tax and collect it from the stockholders by deducting it from its net profits or dividends. In some States are to be found constitutional prohibitions against double taxation, and it is a serious question whether the taxation of the capital stock in the hands of the stockholders, and also as an arbitrary item of taxable value belonging to the corporation does not constitute double taxation. The weight of authority so regards it. Where no constitutional provision prevents double taxation this is possible, although the courts always construe laws, if possible, so as to prevent it.

§ 47. Methods of Taxation. The four elements of taxable value in a corporation were stated in a preceding section. The methods employed in taxing either one or all of these vary in the different States. Where, by statute, the franchises of the corporation are taxed, some procedure is also provided for the establishment of their value. It might be suggested that where the franchises of a corporation, whether the term is used in its primary or secondary sense, are by statute made elements of taxable value and taxed, in proceedings to ascertain the value of the property invested in a plant for the determination of the question of a reasonable charge made by that corporation for services, a value of the franchises at least equivalent to the taxable value should be included as a part of the capital or the

property invested. A distinction is made by the courts between the taxation of franchises and the levy of a tax on the capital stock of a corporation. The taxation of both has been held not to constitute double taxation.

Various methods are employed to determine the value of the capital stock of a corporation for the purposes of taxation. The reader is referred, for illustration, to the statutes of his own State. In some instances, a tax is levied upon the par value of the stock; in other cases, upon the market value at the time its assessed value is ascertained. In still others, the tax is levied upon the amount of the capital stock named in the articles of incorporation. In some States the capital stock of different corporations is classified and assessed according to the dividends paid, a greater taxable value being placed upon the stock of corporations paying the larger dividends.

The tangible value of the property of a corporation is ascertained according to the methods provided by statute and varies, naturally, in the different States. The total amount subject to taxation is fixed at the value of the property less, in some cases, the property exempt from taxation, property otherwise taxed, and, in many cases, the tangible value of the property less the debts of the corporation. Instead of taxing the actual tangible property of a corporation, this result is often accomplished through the taxation of the dividends, the gross receipts, or the net earnings or profits of the corporation. The reader is referred to the statutes of a particular State for the details establishing the methods and procedure followed by that State in the taxation of corporate property.

The shares of capital stock in the hands of the stockholders is distinguished from the capital stock of the corporation and is subject to taxation as their personal property, even where the tangible property of the corporation has already paid a corporate tax, and, perhaps in addition a tax has been levied and collected upon the capital stock of the corporation in its own hands. Some States, however, provide an exemption from taxation of the shares

of capital stock owned by a private individual residing within the State where these shares of stock constitute a part of the capital stock of a domestic corporation.

§ 48. Limitations Upon the Power of Taxation. While, as a matter of theory, the State can exercise its powers of taxation without limit in this country, as said by Judge Cooley: "Government was not organized for the purpose of taxation." Limitations upon an exercise of the power are to be found in both the Federal and State Constitutions. The agencies of the Federal Government are exempt from taxation by the State. Chief Justice Marshall, in McCulloch v. Maryland,[8] held that the power to tax was the power to destroy, and that if the right of a State to tax agencies of the Federal Government was conceded, it would be possible for the States to impair the efficiency and even to destroy the sovereignty of the Federal Government. The converse of the rule also is true, and the courts have held that it is without the power of the Federal Government to tax the agencies of the separate States employed by them in the exercise of their governmental functions or duties. This rule is stated here for the reason that in some instances the agencies of both the Federal and the State governments have been corporations. National banks organized under the present national banking law are, in respect to the issue of currency, regarded as agencies of the Federal Government, for to the United States is given by the Constitution the sole power of coining money and the States are prohibited from emitting bills of credit. Bonds or other securities issued by the Federal Government are clearly beyond reach of the taxing power of the States.

The provisions of the Federal Constitution with reference to the taking of property without due process of law; the appropriation of private property for a public use without the payment of just compensation; the equal protection of the laws; and the impairment of a contract obligation have all been held by the United States Supreme Court as limitations upon the taxing power of the State where an

[8] 4 Wheaton 316.

attempted exercise of that power results in a violation of these constitutional provisions. The Federal Constitution also provides that "no State, without the consent of Congress, shall lay any impost or duties on imports or exports, except what shall be absolutely necessary for executing its inspection laws". Private corporations and their property have been repeatedly held to be persons and within the meaning of these constitutional prohibitions and protective limitations. The courts have held, however, that the States may discriminate in the exercise of their taxing powers between domestic and foreign corporations without acting in contravention of the provisions named above.

Further Limitations Upon the Power to Tax. Several limitations operating both as against the Federal Government and the different States have been stated in the preceding section. There are others of sufficient importance to justify a reference to them in even an elementary work on the subject of private corporations. The taxing power of the United States is derived from direct grants in the Federal Constitution. The taxing power of each of the different States is limited by the prohibitions contained in the Federal Constitution and also such restrictions as may be found in their own constitutions. By the Federal Constitution, the exclusive power is given to the Federal Government of regulating interstate commerce, and it has been repeatedly held that the State may, in an attempted exercise of its taxing power, effect a regulation of interstate commerce, and this action on the part of the State will be, therefore, held unconstitutional.

The usual corporate agencies engaged in interstate commerce are common carriers, telegraph, telephone, and express companies. In respect to the business of an interstate character transacted by these corporations, as well as others, they are all regarded as instrumentalities of commerce and subject to the exclusive control and regulation of Congress. Taxes of a general nature, license or franchise fees, cannot be imposed, where the result amounts to a regulation of their interstate business. The principle

is sufficiently illustrated by a recent case in the Supreme Court of the United States.[4] A statute of Kansas provided, among other things, that before a corporation of another State, even one engaged in interstate business, should have authority to do local business in Kansas, it should pay for the benefit of the permanent school fund a charter fee upon its entire capital stock at a prescribed rate. The Western Union Telegraph Company, a New York corporation, engaged in commerce among the States and in foreign countries, had a capital stock of $100,000,000. It refused to pay the required fee and thereupon the State brought a suit in one of its own courts against the telegraph company and sought a decree ousting and restraining the company from doing any local business in Kansas. The State court gave the relief asked for.[5] The Supreme Court of the United States, however, reversed the judgment of the State court, and held upon the question above involved that the rule, that a State court may exclude foreign corporations from its limits, or impose such terms and conditions upon their doing business therein as it deems consistent with public policy, does not apply to foreign corporations engaged in interstate commerce, and the requirement that the telegraph company pay a given per cent of all its capital, representing all its business, interests, and property everywhere within and outside of the State, operated as a burden and tax on the interstate business of the company, as well as a tax on its property beyond the limits of the State which it could not tax consistently with the due process of law enjoined by the fourteenth amendment. The court also held that the right to carry on interstate commerce was not a privilege granted by the States, but a constitutional right of every citizen of the United States, and that Congress alone could limit the right of corporations to engage therein. And that the disavowal by a State enacting a regulation, of intent to burden or regulate inter-

[4] Western Union Telegraph Company v. State of Kansas *ex rel*, 216 U. S., 1, decided Jan. 17, 1910.

[5] 75 Kansas, 609.

state commerce, could not conclude the question of fact of whether a burden was actually imposed thereby; and that whatever the purpose of a statute, it is unconstitutional if, when reasonably interpreted, it does directly or by necessary operation burden interstate commerce. And, further, that in determining whether a statute does or does not burden interstate commerce, the court would look beyond mere form and consider the substance of things.

§ 49. State Taxation of National Banks. National banks are created solely under and by virtue of the laws of the Federal Government and have, as one of the express objects of their creation, the emitting of bills of credit; the States, by the Federal Constitution, are prohibited from exercising this power. They are to be regarded, therefore, as agencies of the Federal Government in respect to which the States cannot exercise their taxing powers. Congress, however, conferred upon the States, by Act of Congress of June 3, 1864, the power to tax National Banks subject to the limitations contained in that act. The phraseology of the prohibition is:

"But the legislature of each State may determine and direct the manner and place of taxing all the shares of the National Banking Associations located within the State, subject only to the two restrictions that the taxation shall not be at a greater rate than is assessed upon their moneyed capital in the hands of individual citizens of such State, and that the shares of any National Banking Association owned by non-residents of any State shall be taxed in the city or town where the bank is located and not elsewhere. Nothing herein shall be construed to exempt the real property of associations from either State, county or municipal taxes to the same extent, according to its value, as other real property is taxed."

The phrase employed in this act, "moneyed capital in the hands of individual citizens," has been subject of judicial construction, notably and necessarily so by the Supreme Court of the United States.[6] The test of the validity

[6] Davenport Bank v. Board, etc., 123 U. S. 83.

of the tax levied by a State upon the property of a National Bank, is whether it materially and injuriously discriminates against the shareholders of National Banks. If this is the effect of an exercise of the taxing power of the State, that act is clearly unconstitutional.

§ 50. Property Subject to Taxation Must Be Within Jurisdiction of Taxing Power. It is an elementary and axiomatic principle that a tax, to be valid, can only be levied upon the property of an individual or of a corporation, within the jurisdiction of the taxing power. The laws of no sovereign have any extra-territorial effect. Personal property, in respect to the exercise of the power of taxation, is subject to the law of the owner's domicil, although, in recent years, as to the personal property of a corporation or its shares of stock, this rule has partly yielded to what some courts term the *lex situs* rule; that is, the law of the place where the property is kept and used. The shares of stock of the corporation may, therefore, be taxed at the place of the domicil of the corporation without reference to the residence of the owner. The personal property of corporations engaged in interstate commerce and used in a State other than that of its creation may be taxed by the State where it is so used. In a case in the Supreme Court of the United States,[7] it was held that the method of taxation adopted by the State of Pennsylvania was an equitable one which took as the basis of assessment such proportion of the capital stock of the company as the number of miles over which it ran cars in the State bore to the whole number of miles in that and other States over which it ran. The court said:

"This was a just and equitable method of assessment and if it were adopted by all the States through which these cars run, the company would be assessed upon the whole value of its capital stock and no more."

§ 51. Exemptions from Taxation. The State or its subordinate agencies, when acting under lawful authority, may

[7] Pullman Palace Car Company v. Penn., 141 U. S. 18.

grant a corporation, either at or subsequent to the time of its incorporation, an exemption of its property from taxation either for a limited time or as to specific portions of it. A grant of this character, if made for a consideration, is usually regarded by the courts as a contract and its obligation is protected by that provision of the Federal Constitution relative to the impairment of contract obligations. Privileges or exemptions of this nature are subject, however, to the rule of strict construction against the grantee, and unless the exemption claimed clearly appears its existence will be denied. A relinquishment or abdication of the taxing power of the State is never to be presumed. The power of taxation is exercised by the State, not only in the levy of general taxes, so termed, and the imposition of license fees as a source of revenue, but also in the collection of a certain form of tax known as a special or local assessment. This is a specific tax levied upon property for the construction of a local improvement, the paving of a street, for example, and the basis of its legality is the reception by the property taxed of a special benefit or advantage equal to the tax imposed. A good illustration of the application of the rule of strict construction will be found in the principle followed by the courts, that a general exemption from taxation of the property of the corporation does not include a release from the payment of special taxes. The property of the corporation, unless exempt for other reasons, will still be subject to the payment of local assessments, or improvement taxes as they are sometimes termed,

CHAPTER VII

CORPORATE POWERS

The term power, as used in connection with corporations, has a somewhat technical significance. In the legal sense the word power, as applied to private corporations, does not mean their ability to act through their various agents, but rather their legal right and authority to so act. It is possible for a corporation to do an act which is in excess of or beyond its powers as the term is properly used. For instance, a bank corporation may contract to buy real estate for investment, although its charter gives it no such power. Such an act is said to be *ultra vires* (beyond its powers) and this subject will be treated in the following chapter.

A corporation is an artificial and juridical person possessing powers and capacities different from those of its members. In order that an artificial person exist, some affirmative act, or its equivalent, of the State is necessary. It is a creature of granted powers unlike a natural person who can exercise powers given to all. A natural person can do all the acts, for he has the capacity, except those prohibited by law. A corporation, on the other hand, can only exercise such powers or capacities as may be given in its charter and which are the result of the grant by the State. It can only exercise such powers, using the word in its proper sense, as are conferred upon it by the sovereign, either by express grant or through necessary implication, and in general it can be said that its implied powers are those which are incidental to its very existence, or those which are necessary and proper for carrying out

the purposes of its creation. In determining whether a corporation has overstepped its legal powers, two theories or principles are followed by the courts in England and in this country. They are known sometimes as the theory or principle of general capacity and that of special capacities. The rule generally adopted in England is that of general capacity. In Pollock on Contracts, page 119, this doctrine is stated in the following language:

"A corporation once constituted has all such powers and capacities of a natural person as in the nature of things can be exercised by an artificial person. Transactions entered into with apparent authority in the name of the corporation are presumably valid and binding, and are invalid only if it can be shown that the legislature has expressly, or by necessary implication, deprived the corporation of the power it naturally would have of entering into them. The question is, therefore, was the corporation forbidden to bind itself by this transaction."

In Ashbury Railroad Company v. Riche, L. R. 7, H. L 653, the following modification of this rule was made:

"Where there is an Act of Parliament creating a corporation for a particular purpose and giving it powers for that particular purpose, what it does not expressly or impliedly authorize is to be taken as prohibited."

The rule of general capacity, stated by Pollock, with the subsequent modification, is generally adopted in England.

In this country, in the Federal courts, the rule or doctrine of special capacities is generally followed, and that is well stated by the Supreme Court of the United States in Thomas v. Railway Company, 101 U. S., 82:

"We take the general doctrine to be in this country, although there may be exceptional cases and some authorities to the contrary, that the powers of corporations organized under legislative statutes are such and such only as those statutes confer. Conceding the rule applicable to all statutes, that what is fairly implied is as much granted as what is expressed, it remains that the charter of a corporation is the measure of its powers and that the

enumeration of these powers implies the exclusion of all others."

In a later case the doctrine was again stated in much the same language,[1] where Justice Gray said:

"The powers of a corporation, like its corporate existence, are derived from the legislature and are not, as in the case of a copartnership, coextensive with the powers of the individuals who compose it. Its charter, therefore, is the measure of its powers and it can lawfully exercise such only as are expressly or impliedly conferred by that instrument. . . .

"The clear result of all these decisions may be summed up thus: The charter of a corporation, ordinarily, in the light of any general laws which may be applicable, is the measure of its powers, and the enumeration of those powers implies the exclusion of others."

It might be said, however, that in many of the State courts the English rule is followed, especially in respect to the transaction of all business relative to the exercise of the ordinary powers of the corporation or which are necessary to carry into effect powers expressly granted.

§ 52. Presumption of a Legal Exercise of Corporate Powers. The presumption of law exists that a corporation is acting within its powers, another phase of the general presumption of law of right doing. Those dealing with a corporation have a right to assume that it is acting within its legal authority, unless the act is clearly in excess of or beyond its charter rights.

Place and Manner of Exercise. It has already been stated that a private corporation is a creature of the State under the laws of which it has been created and that it can have no legal existence outside the jurisdiction of that State. However, the principle or law of comity, as it is termed, is followed almost universally, and corporations are permitted, through its recognition to engage in the transaction of business elsewhere. They are there subject, however, to all the laws and regulations that may be passed

[1] Central Transportation Company v. Pullman Palace Car Co., 139 U. S., 4.

or adopted by that State relative to the doing of business by foreign corporations, and the courts have repeatedly held that restrictions or limitations upon the right of foreign corporations to so engage in business are not to be regarded as discriminations or a denial of the equal privileges, when compared with domestic corporations, which are prohibited by the Constitution of the United States and its amendments.

It is scarcely necessary to suggest that since a corporation is an artificial person authorized only to transact its business by the State, statutory, and constitutional provisions relative to the manner in which its corporate capacities are to be exercised, control. Furthermore, a corporation is not limited by the statutory term of its existence, but may enter into contracts extending beyond its natural life.

§ 53. Classification and Definition of Powers. The term power has already been defined, and the classification suggested by Chief Justice Marshall in his definition of a corporation in the Dartmouth College case is that generally followed. Their powers are commonly divided into express and implied; those directly and clearly given in the charter and others not expressly granted but which the courts hold may be impliedly exercised. Where a legal authority to do an act, to exercise a power is expressly granted, there can be no controversy as to its legal powers or capacities in this respect.

Implied powers are usually divided into those which the corporation impliedly can exercise because essential or necessary to corporate existence, and those which the corporation can exercise because they are necessary or proper to the exercise of the powers expressly conferred. There is, as a rule, little controversy in respect to the rights of a corporation to exercise the implied powers of the first class, viz, those which are absolutely necessary or essential to the existence of the corporation or the transaction of business, the right to transact which has been expressly given. The disagreement in the authorities chiefly arises in respect to the exercise of the implied powers of a corporation of

the latter class, viz, those which it is claimed the corporation can exercise because they are necessary or proper to the exercise of powers expressly conferred. The contest is over the meaning of the words "necessary and proper". The case of McCulloch v. Maryland, 4 Wheat., 316, will be found of great assistance in determining this question. There one of the questions arising was the significance of the words "necessary and proper" as used in the Federal Constitution in connection with the powers exercised by the Federal Government. The argument and the reasons given by the court can be applied equally to the powers of the corporation. Chief Justice Marshall said, in the course of his opinion:

"Congress is not empowered by it (the Constitution) to make all laws which may have relation to the powers conferred upon the Government, but such only as may be 'necessary and proper' for carrying them into execution. The word 'necessary' is considered as controlling the whole sentence and as limiting the right to pass laws for the execution of the granted powers to such as are indispensable and without which the power would be nugatory; that it excludes the choice of means and leaves to Congress in each case, that only which is most direct and simple. Is it true that this is the sense in which the word 'necessary' is always used? Does it always import an absolute physical necessity so strong that one thing to which another may be termed necessary can not exist without that other? We think it does not. If reference be had to its use in the common affairs of the world, or in approved authors, we find that it frequently imports no more than that one thing is convenient or useful or essential to another. To employ the means necessary to an end is generally understood as employing any means calculated to produce the end, and not as being confined to those single means, without which the end would be entirely unattainable. Such is the character of human language, that no word conveys to the mind, in all situations, one single definite idea; and nothing is more common than to use words in a figurative sense. Almost all compositions contain words which, taken in their rigorous sense, would convey a meaning different from that which is obviously intended. It is essential to just con-

struction, that many words which import something excessive should be understood in a more mitigated sense, in that sense which common usage justifies. The word 'necessary' is of this description. It has not a fixed character peculiar to itself. It admits of all degrees of comparison, and is often connected with other words which increase or diminish the impression the mind receives of the urgency it imports. A thing may be necessary, very necessary, absolutely or indispensably necessary. To no mind would the same idea be conveyed by these several phrases."

In many cases the answer to the query whether a certain act of a corporation is included in the second class of the implied powers, will depend upon the attitude of a particular court upon the question, whether it thinks the proposed act, power or capacity of the corporation desirable, and, further, whether it believes in extending or narrowing the powers of the corporation. The same act or power may be regarded as desirable by some courts and undesirable by others; and the latter may also believe in the general doctrine of narrowing or restricting the powers of the corporation. The answer to the query then will be in the negative. The right to exercise the power will be denied. However, under the doctrine of implied powers, some principles have been adopted which are universally followed. The act, in order that the power to do it may be implied, so it has been held, must tend directly and immediately, not slightly or remotely, to accomplish the objects for which the corporation was created. The word necessary, when the claim is made that the act is necessary to the existence of the corporation, does not always mean an absolute necessity, but merely proper, convenient and reasonably necessary. An incidental or implied power has been defined as "one that is directly and immediately appropriate to the execution of the specific powers expressly granted, and is bounded by the purpose of the corporate enterprise and by the terms and intentions of the charter."[2] Under these principles, it has been held that a corporation cannot engage in a business different from that authorized by its charter.

[2] Beach on Corporations, § 385.

A corporation organized for the purpose of booming logs cannot drive them; one chartered to manufacture lumber cannot construct houses with its surplus product; a railroad organized to conduct the business of a common carrier cannot speculate in townsites. A bank cannot act in the capacity of broker in buying and selling bonds for its customers; and an accident insurance company, it was held, could not insure generally against other casualties than accidents.

In an Illinois Railway Co. case v. Marseilles 84 Ill. 145, it was said:

"The rule is familiar and is not contested that such bodies (private corporations) can only exercise such powers as may be conferred by the legislative body creating them either by express terms or by necessary implication; and the implied powers are presumed to exist to enable such bodies to carry out the express powers granted and to accomplish the purposes of their creation."

In a New Jersey case, New Jersey Railroad Company, etc., v. Hancock, 35 N. J. Law, 545, the same principle was expressed when the court said:

"Power necessary to a corporation does not mean simply power which is indispensable. Such phraseology has never been interpreted in so narrow a sense. There are few powers which are, in the strict sense, absolutely necessary to those artificial persons, and to concede to them powers only of such a character, while it might not entirely paralyze, would very greatly embarrass their operations. Such, in similar cases, has never been the legal acceptation of this term. A power which is obviously appropriate and convenient to carry into effect the franchise granted has always been deemed a necessary one. . . . The term comprises a grant of the right to use all the means suitable and proper to accomplish the end which the legislature had in view at the time of the enactment of the charter."

And in a Connecticut case the court said:[3]

"While a corporation has no powers except those which are conferred by its charter, it is not requisite that those

[3] Hope Mutual Life Insurance Company v. Weed, 28 Conn., 51.

powers should be expressly granted, but it possesses impliedly and incidentally all such powers as are necessary for the purpose of carrying into effect those which are expressly granted. The creation of a corporation for a specified purpose implies a power to use the means necessary to effect that purpose."

§ 54. Common-Law Powers, So-Called. The old text books and cases refer frequently to the existence of certain incidental or implied powers in a corporation which it could exercise even when not expressly granted. These are known as the common law capacities or powers and are: (1) To have perpetual succession; (2) To sue or be sued; to implead or be impleaded, grant or receive by its chartered name and do all other acts that natural persons may; (3) To purchase lands and hold them for the benefit of themselves and their successors; (4) To have a common seal; (5) To make by-laws or private statutes for the better government of the corporation.[4] In an early case in New York considering the powers and nature of private corporations, an opinion was rendered by Justice Nelson, who subsequently became a member of the Supreme Court of the United States. He there reduced these common law capacities, from the standpoint of that day, from five to three, viz, (1) To have perpetual succession; (2) To take and grant property, contract obligations, and to sue and be sued by its corporate name as an individual; (3) To receive and enjoy in common grants of privileges and immunities.[5]

§ 55. Principles of Construction. The charter of a corporation, using the term in its broadest significance, is the source of its powers. The cardinal principles of construction have already been given in preceding sections discussing the charter of the corporation and its interpretation. The general doctrine in respect to the powers of corporations has been stated by the Supreme Court of the United States, Thomas v. Railroad Company, 101 U. S., 82, in the following language:

[4] Bl. Comm., 416.

[5] Thomas v. Dakin, 22 Wend., N. Y., R.

"We take the general doctrine to be in this country, although there may be exceptional cases and some authorities to the contrary, that the powers of corporations organized under legislative statutes are such and such only as those statutes confer. Conceding the rule applicable to all statutes that what is fairly implied is as much granted as what is expressed, it remains that the charter of a corporation is the measure of its powers and that the enumeration of these powers implies the exclusion of all others."

A clear distinction can be made between the exercise of the ordinary and usual business powers of a corporation and those which involve the right of possessing and enjoying extraordinary or special privileges and exemptions. The common rule applied in respect to the former class of powers is the liberal one, or of reasonable and progressive construction, as the phrase was used in Thompson on Corporations. It is true that a corporation can exercise no powers not fairly expressed or implied in the charter, but, on the other hand, it is not the duty of the courts, nor do they attempt to avail themselves of every opportunity or of finding means on every occasion to defeat or impair the effect of the apparent language of the charter. Corporate powers are to be construed fairly and reasonably. On the other hand, where the question of the right to exercise an exclusive power, privilege or exemption is claimed, the language upon which such a power is based is to be construed strictly, and nothing, the courts hold, will pass by implication. In a Massachusetts case[6] it was said:

"We know of no rule or principle by which an act creating a corporation for certain specific objects, or to carry on a particular trade or business, is to be strictly construed as prohibitory of all other dealings or transactions not coming within the exact scope of those designated. Undoubtedly, the main business of the corporation is to be confined to that class of operations which properly appertain to the general purposes for which its charter was granted; but it may also enter into contracts and engage in transactions which are incidental or auxiliary to its main business, or

[6] Brown v. Winnisimmet Co., 11 Allen, Mass., 326.

which may become necessary, expedient, or profitable in the care and management of the property which it is authorized to hold under the act by which it was created."

And in Downing v. Road Company, 40 New Hamp. 230, the court stated as a rule of construction:

"In giving a construction to the powers of a corporation, the language of the charter should in general be construed neither strictly nor liberally, but according to the fair and natural import of it, with reference to the purposes and objects of the corporation. If the powers conferred are against common right, and trench in any way upon the privileges of other citizens, they are, in cases of doubt, to be construed strictly, but not so as to impair or defeat the objects of the incorporation."

The rule of strict construction, in all its severity, was stated by the Supreme Court of the United States[7] in the following language:

"The rule of construction in this class of cases is that it shall be most strongly against the corporation. Every reasonable doubt is to be resolved adversely. Nothing is to be taken as conceded, but what is given in unmistakable terms or by implication equally clear. The affirmative must be shown. Silence is negation and doubt is fatal to the claim. This doctrine is vital to the public welfare. It is axiomatic in the jurisprudence of this court."

Concrete Illustrations of Implied Powers. The common incidental or implied powers have been stated in a previous section, but a brief discussion of them may assist the reader to a better understanding of their nature and extent.

§ 56. Perpetual Succession. The right of perpetual succession is an essential characteristic and power of a private corporation. Its possession enables the corporation to maintain its legal identity as an artificial person during the term of its continuance. By the term perpetual is understood not necessarily enduring forever in the common acceptation of the term, but simply for that length of time

[7] Northwestern Fertilizing Company v. Village of Hyde Park, 96 U. S., 659.

which the corporation is permitted to exist under the laws of the State creating it. Some charters originally were granted giving to the corporation a perpetual life in the exact sense of the word. It is a common and universal practice now for the creating power to limit the duration of the existence of the corporation, and the term perpetual succession, therefore, means simply, as already stated, the right of a corporation to exist during the period limited by law. This characteristic of perpetual succession, using the term as above limited, is one of the principal distinguishing features of a private corporation as compared with a natural person or a group of natural persons acting under any form other than that of a corporation. The corporation maintains its identity during its life, irrespective of the death of its members. These may be constantly changing, by death or transfer of interest, and yet the artificial person exists as a legal person. Blackstone compared the corporation in this respect to the River Thames, which he said remained the same at any given point, although the particles of water which composed it were constantly changing.

§ 57. **A Common Seal.** The implied right of a corporation to use a common seal undoubtedly had its origin in the universal use by natural persons, under the common law, of a seal, the custom based upon the inability of many to write. The use of the seal was a requisite to the legal act of a natural person and this principle was naturally applied to artificial persons as they were created. This rule has been so modified that a corporation may legally act without a seal in all cases where an individual may do so, unless especially required by some statutory provision.

§ 58. **Power to Make By-Laws.** Another implied or common law capacity, so-called, is the power to make by-laws. A by-law has been defined as "a rule of permanent character adopted by a corporation for the regulation of its internal affairs." Its purpose is to regulate the conduct of the business of the corporation and to define the duties of its various officers and agents. The right to

adopt by-laws is usually vested in the members or the stockholders of the corporation, unless by the articles of incorporation this power is given to the board of directors. It is axiomatic that the existence of the right, whether in the members of the corporation or its board of directors or managing officers, creates the coextensive power, in the proper and legal manner, of amending or repealing them. The provisions of the charter, or of the general laws of the State, if they exist, must be strictly observed in the adoption, the amendment, or the repeal of by-laws.

Upon Whom Binding. It may be important to know at times the legal effect of a by-law upon the corporation itself or those dealing with it, and this condition is suggested by the title of this paragraph. The corporation clearly is bound and the members of the corporation; also those dealing with the corporation and having actual notice of the existence of a by-law which may affect the legal results of a business transaction. The members of a corporation are bound by the by-laws at all times and under all conditions, even though they have no actual notice or knowledge of their existence. If actual notice or knowledge is lacking, the courts hold that because of the fact of membership the principle of constructive notice or knowledge is applied. Constructive notice or knowledge is that which is imputed to the person himself, or which he necessarily ought to know, or which, by the exercise of ordinary diligence, he might know. The legal effect of by-laws, their interpretation and construction, is a judicial function, and one exercised, therefore, by courts of competent jurisdiction.

Requirements of a Legal By-Law. A by-law, it has already been stated, is a rule of permanent conduct controlling the action of the corporation and of its members and officers in the management of its affairs. It is, therefore, a law, though limited in its scope and application. The by-law, to operate legally as a rule of conduct, must possess all the characteristics of a law. The charter of the corporation is its superior and paramount law, and it follows

that a by-law cannot be inconsistent with or contravene any of its provisions or terms. The Constitution of a State or of the United States is the superior and paramount law, and the act of any subordinate body cannot be contrary to its provisions. A by-law cannot impair a vested right. It must not conflict with the general principles of the common law where they control, or be repugnant to laws of the State. A by-law of a corporation fixing a penalty for the doing of an act by its members greater than the penalty provided by the general laws of the State for the commission of the same act, was held invalid. A by-law cannot have a retroactive effect, a principle which applies universally to all legislation. By-laws must be reasonable and not oppressive; neither can they operate in restraint of trade or be against the public policy. The latter phrase has been defined as follows: "By public policy is intended that principle of the law which holds that no subject can lawfully do that which has a tendency to be injurious to the public or against the public good."[8] It is a term which is indefinite both in its meaning and application, and should be adopted as a reason for a legal holding only when all other reasons fail, for, as was said by an eminent English judge many years ago, the adoption of this as a legal reason for a decision is like "mounting an unruly horse; one never knows where it will land him." They must be general and not for the benefit of or detrimental to any particular member or class of members; they must be uniform in their application, principles also applying to all legislation.

As illustrative of the principles above referred to, some cases may be noted. A by-law requiring, in the absence of a charter provision to that effect, the consent of the president of the corporation to a transfer of stock was held void as in restraint of trade, but by-laws requiring the surrender of a certificate of stock to certain designated officers of the corporation, and its cancellation by them, in case of sale and transfer of stock, have been usually sustained as valid and not unreasonable nor in restraint of

[8] Greenwood on Public Policy.

trade. A by-law of a corporation requiring as a qualification for membership a prohibition against membership in the militia was held invalid, as in contravention of the law of the land. By-laws of social clubs, chambers of commerce, boards of trade, and similar bodies providing for the expulsion of members for dishonorable conduct and prohibiting the transfer of membership, so long as the member may be indebted to the corporation or to any other member, have been held valid.

§ 59. By-Laws Restricting Powers of Corporate Officers and Agents. A corporation being an artificial person necessarily must act through natural persons, its agents. The adoption of by-laws defining and establishing the powers of corporate officers and agents is a common custom. In many cases they restrict or limit the power of the agent when acting for the principal, viz, the corporation. The authorities are conflicting upon the question of the effect of a restrictive by-law as between third persons dealing with the corporation and the corporate agents acting in its behalf. This is especially true where the third person has the legal right to presume from the indices of authority or the title of a corporate officer or agent, with whom he is dealing, that the transaction in question comes within the general or apparent scope of the authority of that corporate agent, and that his act, therefore, is binding upon the principal. As stated in a preceding section, the by-laws of a corporation are not binding upon third persons dealing with the corporation unless they have actual notice or knowledge of the by-law and act upon that knowledge. The weight of authority inclines to the view that a by-law which limits the authority of a corporate agent will not affect the legality of the transaction, where he acts within the apparent scope of his power and authority, though in excess of his actual authority as fixed by the by-law. There are authorities, however, which hold to the contrary. The sounder reasons support the weight of authority, for, as was said in a recent New York case:[9]

[9] Rathbun v. Snow, 123 N. Y., 343.

"The defense based upon a limitation in the by-laws of the company, of which the plaintiff had no knowledge, cannot be sustained. By-laws of business corporations are, as to third persons, private regulations, binding as between the corporation and its members, or third persons having knowledge of them, but of no force as limitations per se as to third persons of an authority which, except for the by-law, would be construed as within the apparent scope of the agency. Third persons may act upon the apparent authority conferred by the principal upon the agent and are bound by secret limitations or instructions qualifying the terms of the written or the verbal appointment."

§ 60. Power to Acquire and Hold Real Estate. At common law, one of the implied or incidental powers of the corporation was "to purchase lands and hold them for the benefit of themselves and their successors." This implied power exists almost universally at the present time where the power to purchase and transfer real property is necessary to the existence of a corporation, or convenient and proper to the purposes for which the corporation was organized. The Minnesota statutes contain a provision which is quite common to the States: "Every corporation formed under the provisions of this chapter shall have power . . . to acquire by purchase or otherwise, and to hold, enjoy, improve, lease, encumber, and convey all real and personal property necessary to the purposes of its organization, subject to the limitations hereafter declared." Independent of a statutory provision of this character, a corporation will have the implied power, under the circumstances first noted in this section, to acquire, hold, and transfer real property.

An Indiana case,[10] in considering the question of the power of private corporations to acquire and alienate real estate, divided them into four classes, as follows: "First, those whose charter or law of creation forbids that they should acquire and hold real estate. In which case a corporation cannot take or hold real estate; and a deed or devise to it passed no title. (Note, however, the discussion on

[10] Hayward v. Davidson, 41 Ind. 212.

the point which follows.) Second, those whose charter or law of creation is silent on the subject. In such case, as a general rule, there is no power to acquire and hold such property. But if the objects for which the corporation was formed cannot be accomplished without acquiring and holding the title to real estate, the power to do so is implied. Third, those corporations whose charter, etc., authorizes them in some cases, or for some purposes, to take and hold the title to real estate. In these cases, as the corporation may for some purposes acquire and hold title, it cannot be questioned by any party, except the State, whether the real estate has been acquired for the authorized purposes or not. Fourth, those whose charter, etc., confer a general power to acquire and hold real estate, such corporations may take and hold real estate as freely and as fully as natural persons."

Limitations upon Power to Acquire. To prevent the acquisition of large tracts of land by corporations, through the English statutes of mortmain, ending with 9 George II., they were forbidden to take and hold real property without a license from the crown. Statutes of this character have not been passed generally in the United States, although recognized in Canada, Great Britain and in Pennsylvania. Statutory or constitutional provisions have been quite commonly adopted throughout the United States by the different States limiting the power of alien corporations to acquire and hold real property. The Minnesota statute is illustrative of this class of laws:[11] "Except as hereinafter provided no person, unless he be a citizen of the United States or has declared his intention to become a citizen, and no corporation, unless created by or under the laws of the United States or of some State thereof, shall hereafter acquire lands or any interest therein except such as may be acquired by devise or inheritance and such as may be held as security for indebtedness. . . . Except as hereinafter provided, no corporation or association, more than twenty per cent of whose stock is owned by persons not

[11] Revised Laws of Minnesota, 1905, §§ 32, 35, *et seq.*

citizens of the United States, or by corporations or associations not created under the laws of the United States or of some State thereof, shall acquire lands in this State."

In the absence of special statutory provisions, there is no limitation in either England or the United States to take real property by devise, though this power, it must be understood, can only be exercised in the acquirement of property for use by the corporation in the conduct of its business as authorized by the general objects of the corporation. The acquisition of real property through any method, for purposes entirely foreign to the business for which the corporation was organized, may be directly and in any case is impliedly forbidden.

Express or implied prohibitions against the acquisition of real property by private corporations does not prevent them, however, from taking lands as a security for a debt due the corporation, or in the satisfaction and payment of a debt, nor do they apply to the acquisition of real property at a foreclosure sale. In determining the power of a corporation to acquire real property under its charter, the rules for the interpretation of charters and the construction of corporate powers, as already stated in preceding sections, must be applied and followed. The courts have held, as illustrating these principles, that a manufacturing corporation may purchase land in an adjoining city upon which to construct and maintain an office building of a size at that time largely in excess of its actual needs.[12]

A manufacturing corporation, it has also been held, may purchase land not only for the purpose of erecting its factories, but also, if it is reasonably necessary, for erecting houses for its employes.[13] A corporation created for charitable purposes and for the promotion of inventions and improvements in the mechanic arts, it was held, had authority to purchase land for the erection of a building for the purpose of holding exhibitions and meetings.[14]

[12] People v. Pullman Palace Car Company, 175 Ill. 125.

[13] Steinway v. Steinway & Sons, 17 Misc. Rep. (N. Y.), 43.

[14] Richardson v. Mass. Charitable and Mechanic Ass'n, 131 Mass. 174.

If the purposes for which a corporation acquires real property are to procure a monopoly, the transaction will be regarded as not only *ultra vires,* but as contrary to public policy and illegal; though, if this power of the corporation is expressly conferred by its charter, the contrary rule will hold.

The power to convey is, of course, coextensive with the power to take and hold subject to the one limitation that a corporation must not grant away or pledge its property and franchises to an extent which will prevent it from carrying out the purpose of its creation. This limitation, however, is almost exclusively applied to those corporations of a quasi-public character.

Title Acquired. In the absence of statutory provisions, and where the corporation is authorized expressly or impliedly to acquire and hold real property, it may exercise its right in the same manner and acquire the same estate which it would be possible for a natural person to acquire under similar circumstances. Where the lawful authority exists, the title acquired may therefore be a fee simple, leasehold interest or an easement merely.

Right to Acquire; How and by Whom Questioned. A corporation may acquire and attempt to hold real property contrary to its charter or to the general principles named in the preceding sections, and the question then arises of its legal title to the property thus acquired and by whom its rights can be questioned. This subject will be more fully discussed under the chapter relating to the *ultra vires* acts of a corporation. It can be stated here, however, that although there are some cases to the contrary, the great weight of modern authority holds that where a corporation has acquired property contrary to an express prohibition or to its charter powers, the title to the real estate so acquired passes to the corporation, and its legal rights in respect thereto can only be questioned by the State.

This principle is obviously based upon the fundamental one that all the powers and capacities of a corporation pro-

ceed from the State. In respect to the acquirement of property, real and personal, no rights are derived from third persons dealing with the corporation. If the corporation has violated a law of the State or of its charter provisions, it is for the State and the State alone to question the legality and the legal effect of such transactions. This rule of law has also been applied on the grounds of public policy, for the adoption of another different one would lead to endless confusion and inconvenience, not only in the transaction of the corporate business, but in respect to real estate titles throughout the land. It follows, therefore, that even where a real estate corporation has acquired and is holding lands contrary to law it may convey a good title for them to a grantee or maintain an action against trespassers. The rights of a corporation to acquire and hold real property cannot be inquired into collaterally or taken advantage of by third persons dealing with the corporation.

§ 61. General Powers as to Property. Within the limitations of the purpose of its creation, and subject to the restrictions already mentioned, a corporation has the same right to acquire and control property, other than real, that a natural person has. At common law there was no restriction placed upon the quantity or the value of the personal property which a corporation might hold, except such limitations as might grow out of the nature of the corporation itself and the purposes of its creation. The statutes of mortmain were never held to apply to personal property. The true rule, at the present time, is that a corporation may purchase and hold or sell personal property without restraint other than that which is generally imposed by law, its charter, and the objects of its creation.

§ 62. Power to Contract. The rules of law relative to the construction of the corporate charter and the extent of its powers apply to the subject of this section. The exercise of corporate powers, in a large measure, involve acts of a contractual nature. The general rule in respect to the validity of a corporate contract is that it is valid.

The presumption of law being in favor of right doing, the contracts of a corporation are presumed to be within the lawful scope and objects of the corporation, until, by a preponderance of proof, the contrary appears. The burden of establishing a corporate contract as *ultra vires* is upon the party making this contention. The courts follow, also, the general principle that, within the limitation of its powers, either express or implied, and in furtherance of the general purposes for which it was created, a corporation may as freely contract as an individual might under like circumstances and conditions.

Formalities to Be Observed in the Execution of Corporate Contracts. At common law the rule was rigidly adhered to that a corporation could legally enter into a contract only by the use of its seal. The corporation "spoke through its seal"; but this rule has been relaxed to such an extent that for many years a corporation has only been required to use its seal when, under the same conditions, its use was obligatory upon natural persons. Justice Story, in an early case in the Supreme Court of the United States,[15] said, after discussing the common law rule:

"The technical doctrine that a corporation could not contract, except under its seal; or, in other words, could not make a promise, if it ever had been fully settled must have been productive of great mischiefs. Indeed, since the doctrine was established that its regularly appointed agent could appoint in their name without seal, it was impossible to support it, for otherwise the party who trusted such contract would be without remedy against the corporation. Accordingly, it would seem to be a sound rule of law that wherever a corporation is acting within the scope of the legitimate purposes of its institution, parol contracts made by its authorized agents are express promises of the corporation; and all duties imposed upon them by law and all benefits conferred at their request raise implied promises for the enforcement of which an action will lie."

The by-laws of the corporation may prescribe certain

[15] Bank of Columbia v. Patterson, 7 Cranch. 298.

formalities to be observed by it in the execution of its contracts. A by-law of this character, it has been held, is not binding upon one who, with no knowledge of its existence, enters into contractual relations with the corporation, and where the officer or agent with whom he is dealing is apparently clothed with full power to bind the corporation. If the third person has knowledge of by-laws limiting the authority of the corporate officers or agents to act, he is clearly bound by this actual knowledge. The courts also hold that third persons dealing with the corporation are bound by the limitations upon its powers contained in the charter of the corporation, though sometimes this rule has been doubted where the charter is a special act of which even a court will not take judicial notice, but which must be specially pleaded. One dealing with a corporation through its agents may rightfully assume that it is acting within its powers and with due observance of the formalities and steps required by its by-laws and its charter, unless the contract itself or the manner of making it is clearly and unmistakably in excess of its corporate powers. Statutory provisions establishing formalities to be observed by corporations in the making of contracts must be observed either strictly or substantially, as the provisions of the law are held to be either mandatory or directory in their character. The authority of corporate officers and agents will be considered in a subsequent chapter.

Ratification and Estoppel. A contract entered into by a corporation in an irregular or informal manner, or one made by a corporate agent in excess of his apparent authority, may subsequently become binding upon the corporation through the doctrine of ratification. This principle will be applied where the corporation subsequently is informed of the existence of the contract and takes no steps to disaffirm it; where, without its recognition, it takes no steps to disaffirm the contract, or where it formally adopts the contract, makes it its own or accepts its benefits. "Authority in the agent of a corporation may be inferred

from the conduct of its officers or from their knowledge or neglect to make objections as well as in the case of individuals."[16]

In the case of irregular, informal, and even unauthorized contracts, the parties may be bound through the doctrine of estoppel. This principle is applied sometimes in those cases where it was represented and assumed by the contracting parties that the capacity to make the contract existed and that its execution was regular and formal, and that all of the provisions of the charter or of the by-laws had been complied with as required. A definition of estoppel was given in a leading case,[17] and may be useful at this time. Lord Denman, in that case, said:

"Where one by his words or his conduct wilfully causes another to believe in the existence of a certain state of things and induces him to act on that belief so as to alter his own previous position, the former is concluded from averring against the latter a different state of things as existing at the same time."

Contracts Void as Against Public Policy. All persons, artificial equally with natural, are forbidden to enter into contracts which the sound policy of the law considers detrimental or injurious to the public interests. This principle applies particularly to corporations of a quasi-public character, and arises from the nature of the privileges or franchises given them by the State. The established principles of the common law may stamp certain contracts with this character, and absolute prohibitions may, in other cases, render them illegal as well as *ultra vires.* Corporate contracts may not only be *ultra vires,* or in excess of their corporate powers, but also illegal for the reasons stated above. A lobbying contract would clearly be illegal as well as *ultra vires,* because involving the use of improper means to influence or prevent legislation. Contracts which effect an unreasonable restraint of trade or tend to create

[16] Sherman v. Fitch, 98 Mass. 59.

[17] Pickard v. Sears, 6 Ad. and El. 469.

a monopoly and prevent competition, whether in violation of well recognized principles of common law, or contrary to the express provisions of some statute, are also illegal and not merely *ultra vires*. Traffic contracts between common carriers, pooling arrangements, contracts securing to a firm exclusive and lower rates, may be illegal because contrary to law. The Interstate Commerce Act and the Sherman Anti-Trust Act, with their various amendments as passed by the Federal Congress, prohibit corporations as well as individuals from making contracts of the character suggested, and are illustrative of this class of statutory regulations.

§ 63. Power to Raise Money. The raising of money is generally recognized as one of the chief objects for which private corporations are formed. The use of capital is indispensable in most cases to the conduct of their business and the exercise of their powers. Two methods are ordinarily employed by a corporation to accomplish this purpose; first, by the issue of its capital stock; and, second, by loan either secured or unsecured. In the case of stock corporations, the charter provides the maximum limit of its capital stock, and if the entire amount has not already been subscribed and paid in, or if the corporation has been duly authorized to increase its capital stock, it may issue new shares and dispose of them for this purpose. It is through the issue of its original capital stock that its first funds are secured for the transaction of its corporate business and the payment of its creditors. The shares of stock are generally sold to shareholders at their par value.

The other method employed by corporations to secure funds for carrying on their corporate business, is through the making of loans, either secured or unsecured. In the absence of express restrictions in its charter, a private corporation may borrow money, the same as a natural person, whenever the nature of its business demands or authorizes it; but it is clear that it cannot do so if the act is unauthorized or if the purpose for which it is organized does not require it. It is common for the State to require

that in articles of incorporation the maximum amount of corporate indebtedness shall be stated. If a provision to this effect exists, the corporation is limited clearly in the maximum indebtedness which it can incur through the borrowing of moneys and whether the loan is secured or unsecured. The necessity for security depends, necessarily, upon the credit of the corporation, the amount of capital invested or employed in the transaction of and the volume of its business. In many instances, a corporation is required to give security for moneys borrowed, which usually consists of a mortgage or pledge upon specific property, or generally upon its entire corporate property and franchises. A private corporation, not of a quasi-public character, ordinarily is not restricted in the extent to which it can mortgage its property and franchises for the purpose of securing a loan. The courts hold, however, that in respect to quasi-public corporations, and especially railway companies, that the corporate power to mortgage the property and the franchises is not an implied one, but must be expressly granted. This principle is based upon the reason that corporations of this character are engaged not only in the carrying on of their business upon private capital and in the capacity of a private corporation, but are also required to perform, because of the nature of their enterprise, certain duties to the public at large. The business of a railroad corporation or common carrier is the transportation of freight and passengers. Because of the nature of this business, they are subject to a greater degree of control and regulation by the State, and it is also regarded as against public policy that they should, by any act of theirs, impair or destroy their ability to perform their public duties. Through the mortgaging of their franchises and property, the courts have held that this result may be attained. The power to mortgage the corporate franchises and property of a quasi-public corporation must be expressly granted.

§ 64. Power as to Own Stock. *By Purchase.* The authorities are conflicting upon the question of the power

of a private corporation to acquire and hold its own stock. There are two well-established lines of decisions, one holding that in the absence of statutory limitations the corporation can acquire, by purchase or otherwise, shares of its own stock, and hold them as a corporate asset. But these decisions further hold that this cannot be done where the effect of such a transaction is to perpetrate a fraud upon or affect the rights of corporate creditors. The other line of cases hold that, independent of statutory provisions, a private corporation cannot so acquire and hold its own stock, the reason being that a transaction of this kind works a fraud upon and substantially affects the rights of the corporate creditors.[18]

By Increase and Decrease. The amount of capital stock of a stock corporation is fixed by the articles of incorporation, and it is well settled that this can neither be increased nor diminished without legislative authority. The power to increase or decrease its stock must be expressly given, and it must be exercised by the stockholders of the corporation, for it is considered one of the extraordinary or fundamental powers of a corporation. Where the capital stock of a corporation is increased, the rule of law generally obtains that the stockholders are entitled to their *pro rata* or proportionate part of the increase at the price fixed for which the stock is to be sold.

Many of the States provide a liability of shareholders, in addition to or in excess of their common law obligations, namely, the par value of their stock. After the reduction of the capital stock of a corporation where an additional stockholders' liability is attached by constitutional or statutory provision, this is not diminished through the reduction. Creditors whose claims have accrued prior to the reduction of the capital stock can look for a payment if the corporate property is insufficient to the original liability of the stockholders. Those whose claims have been created subsequent to the reduction can only enforce a

[18] Clapp v. Peterson, 124 Ill. 26; Coppin v. Greenlees Co., 38 O. St. 275.

stockholders' liability as based upon the reduced capital stock.

§ 65. Power as to Negotiable Instruments. The general rule in this country is that a corporation organized for pecuniary profit has the implied power to make, draw, accept, or endorse negotiable instruments in furtherance of and when within the scope of its corporate business. If these acts are foreign to the purposes for which the corporation was created, or contrary to the terms of its charter, they cannot be sustained. A corporation has, however, no implied power to lend its credit by becoming a party to a note or bill for the mere accommodation of another, though that act may be, indirectly, beneficial to the corporation itself. An accommodation note or bill may be enforced, if it passes into the hands of a *bona fide* holder, without notice of its character, and when within the apparent scope of the powers and authority of the corporation. The courts have also held that an accommodation endorsement may be enforced if all of the stockholders consent.

§ 66. Power to Guarantee Bonds. It is customary for railroad corporations to guarantee, in many cases, the bonds of subsidiary and auxiliary companies. This power must be expressly conferred and cannot, as a rule, be implied. The principle is based primarily upon the reason that it is inexpedient to permit a corporation to subject itself and its stockholders to the risks involved, which necessarily follow a transaction of this character, and the further reason that, especially in the case of quasi-public corporations, results might be accomplished contrary to public policy or some express statutory provision. In some cases, where the organization of a subsidiary line is convenient and proper, and in furtherance of the objects for which the corporation was created, it has been held that in the absence of statutory prohibitions the implied power may exist. It is necessary, however, to the validity of the transaction, that the company so guaranteeing the bonds or securities of another receive a consideration which may be a deposit of stock as collateral. Ownership of

the stock or the general benefit and advantages derived from the control of the subsidiary line would also be a consideration.

§ 67. Power to Execute and Issue Bonds. As a means of raising money, and in the absence of express restrictions, a corporation has the implied power to execute and issue bonds for its legitimate corporate purposes. These may be issued in any form or contain any provisions not prohibited by its charter, using the term in its broad sense, which includes, it will be remembered, general statutes applicable to that class of corporations. Bonds issued by a corporation are regarded as negotiable instruments, whenever the intent to make them so is to be gathered from their form and the manner in which they are put in circulation. Statutory provisions, if such exist, in respect to the form, time of payment, or amount, must be complied with; and the rule also obtains, as already suggested, that no corporation can lawfully issue its negotiable securities, including bonds, for a purpose which is foreign to the objects for which it is created. Unless prohibited by law, it may issue and sell them at a discount. In some States, in order to prevent a fictitious issue of indebtedness, statutes have been passed prohibiting the issue of securities, except for money paid, labor done or property actually received by the corporation, and further providing that corporate obligations issued contrary to such provisions shall be void and indebtedness thus created unenforcible. These statutes, however, are liberally construed in favor of the corporation, and the fraudulent character of such indebtedness must be clearly established. It is a well recognized principle that many corporations, especially at the time of their organization, and those whose credit has become involved, cannot sell their securities for the highest price obtainable. They are not prohibited, under such circumstances, from issuing their securities and disposing of them at the best possible price, which may be less than par.[19] Where securities are issued representing property

[19] Handley v. Stutz, 139 U. S. 417.

received or services rendered, it is sufficient if a fair and reasonable value is placed upon the latter for the obligations issued in exchange. The fair and reasonable value of the service rendered or the property received at the time of the exchange establishes the good faith of the transaction, and it will not be regarded as fraudulent in its character if subsequently the property so received materially depreciates in value.

§ 68. Power of Eminent Domain. The power of eminent domain is a sovereign right inherent, inextinguishable and continuing in its nature. It is that power of the State to appropriate or take private property for a public use upon the payment of just compensation to the owner which, it has been held, must be full, ample, just, and complete. Constitutional provisions protect the private owner in the possession and use of his property against the exercise of the power without the payment of this just compensation. The State can exercise the power of eminent domain or, it has been held, it may lawfully delegate the right to such agencies as it may select. The limitation, however, exists in all cases of delegation that private property can be taken for only a public use. The right to exercise this power by a private corporation, it will be noted from the preceding, is limited to those of a quasi-public character. Public corporations, common carriers, and other corporate organizations of a like character are the agencies to which the right of an exercise of the power is usually delegated by the State, and it must be conferred in express terms. It can never be implied. Its exercise by a corporation to whom the power is delegated must be in conformity with statutory and constitutional provisions; and a few of the essential principles controlling will be noted in the following sections.

Essentials of a Legal Exercise of the Power. Upon an examination of constitutional phrases granting and limiting an exercise of the power of eminent domain, it will be noted that three words or phrases are used which have been the occasion for judicial construction by many courts.

These are, taking them in their orders: "property", "taken" or "taking", and "public use".

Property, Definition Of. "The word commonly used in connection with the exercise of the power of eminent domain is 'property' and this suggests the question, what is property? A correct determination of the meaning of the word is important, for if the thing taken be not legally considered property, clearly the owner is not entitled to compensation and an exercise of the power is not necessary. The most satisfactory definition of property is that given by Jeremy Bentham in which he says: 'The integral or entire right of property includes four particulars: (1) right of occupation; (2) right of excluding others; (3) right of disposition or the right of transferring the integral right to other persons; (4) right of transmission in virtue of which the integral right is often transmitted after the death of the proprietor without any disposition on his part to those in whose possession he would have wished to place it.' Or, summarized, the rights of occupation, exclusion, disposition, and transmission. Property, therefore, consists not in the thing or the subject of a right itself, but of rights in things created, sanctioned and protected by law. Formerly, a narrow and restricted meaning was attached to the word 'property' and the property owner was, therefore, restricted in the amount of compensation which he might recover. The modern tendency is towards a liberal construction of the word and the right of compensation is correspondingly enlarged."[20]

Taking or Taken, Definition Of. "The word 'taking' or 'taken' was the one originally and most commonly used in statutory or constitutional provisions relative to the exercise of the power of eminent domain. The extent of compensation to which one is entitled and the proper exercise of the power depend upon what is taken and whether there is a taking. The early meaning given to the word under discussion embodied the idea that before compensation could be recovered by the individual or in order to consti-

[20] Abbott, Public Corporations, § 431.

tute a taking, there must be an actual physical dispossession of the thing taken from its original owner. This meaning was probably based upon a narrow construction of the word 'property', but with the adoption of a broader interpretation of that word, the meaning of the word 'taking' has been correspondingly enlarged; and the modern view is that to constitute a taking an actual physical divesting or dispossession of property is not necessary, but a damage to or deprivation of any of the essential rights of property will be sufficient to constitute a taking and entitle the owner to compensation under the constitutional provision. These essential rights have already been stated as being those of occupation, exclusion, disposition, and transmission."[21]

Various phrases in addition to or in connection with the words "taking" or "taken" will be found used in the Constitutions of different States. These phrases, as thus variously used, and including such words as "damages", "injured", or "injuriously affected" are intended to enlarge the right to compensation, and they include physical injuries not held to be "a taking" within the strict meaning of those words.

Public Use, Definition Of. What is a public use is a question for the judiciary and no problem has ever been submitted to the courts upon which there is a greater variety and conflict of reasoning and results than that presented as to the meaning of the words "public use" as found in the different State constitutions regulating the right of eminent domain.[22]

"The power of eminent domain is authorized only when property is to be taken for a public use; it cannot be exercised for a mere private purpose. The State has no power even when compensation is paid in full, in any case, to divest an individual of his property and grant it to another without some reference to a use to which it is to be appropriated for the public benefit. What is a public use is a judicial question and one upon which

[21] Abbott, Public Corporations, § 437.

[22] Dayton Mining Co. v. Seawell, 11 Nev. 394.

there is a great variety and conflict of reasoning and results. The question of public use is not affected by the character of the agency employed. The query is what are the objects or results to be accomplished, not who are the instruments or agencies selected by the sovereign for attaining this. Neither is the question of public use affected or determined by the fact that the use or the benefit is local or limited, nor is it determined by the necessity or the lack of necessity for the condemnation; neither is it established by the frequency or the infrequency of the use.

"There are two theories in respect to the proper and legal meaning of the words 'public use' as used in constitutions or legislative enactments. The first might be termed the theory of strict construction, and it maintains the principle that for a public use to exist there must be a literal use or right of use on the part of the public generally, or limited portion of it, without the payment of compensation for the exercise of this use or right of use.

"The second theory is based upon a liberal interpretation of the words 'public use' and holds that the words are equivalent to public benefit, utility or advantage, and are not limited by the actual use by the public of the property taken or some limited portion of it. The modern construction of the words seems to be in favor of the second or liberal interpretation and of an equivalent meaning of use by the public." [23]

Construction of Right to Exercise. Through the exercise of the power of eminent domain by the State or any of its delegated agencies, the private property of an individual is arbitrarily and forcibly taken to supply the demands of some great and urgent public need. It is axiomatic to state that under these circumstances the authority to exercise the power must be strictly followed. The condition precedent to the valid exercise of the power as prescribed by the action of the legislative body must be strictly construed, the authority must be expressly given and the manner of its exercise, as provided by law, strictly followed. All statu-

[23] Abbott, Public Corporations, § 435.

tory requirements are considered essential. The fact that they are prescribed by law in connection with an exercise of the power stamps them with this character and not their relative importance. It is not for the courts to say that because a statutory provision is apparently unimportant or relates to a matter of detail that it is not essential.

Notice to Property Owner. So far as the owner of property to be condemned is affected, his only concern is the just compensation to which he is entitled, and it is fundamental in connection with property interests that a person cannot be legally or justly deprived of them without notice to him of the action leading to this result. It is, therefore, a jurisdictional condition that the owner whose property is sought to be taken must be apprised in some way of the pendency of the proceedings through which this end is sought to be attained. It is a prerogative for a law-making body to determine the character and extent of the notice necessary, but the legality of its action will be measured in this respect by that constitutional provision which prohibits the taking of property without due process of law. A New York case decided that "due process of law requires that a person shall have reasonable notice and a reasonable opportunity to be heard before an impartial tribunal before any binding decree can be passed affecting his right to liberty or property." Notice is universally regarded as one of the essentials of due process of law. It need not be, however, in all cases actual, and in fact in many instances where the power is exercised by public corporations for the purpose of establishing highways, and streets, constructive notice alone is given and is regarded by the courts as sufficient. Statutory requirements as to the manner in which notice must be served upon the property owner must be strictly followed, and it has been held that the absence of a requirement calling for the service of notice does not relieve one exercising the power of eminent domain from giving notice. Many cases hold that independent of statutory provisions, the fundamental provision obtains that private property can not be taken with-

out due process of law, and this included, as stated above, as one of its prime essentials, the giving of notice.

§ 69. **Miscellaneous Powers.** A corporation has no implied power to become a surety or guarantor for the debts, defaults, or acts of another. These powers must be expressly conferred by the charter. Corporations have no implied power to enter into a partnership with individuals or other corporations, or into agreements which substantially create the relation of a partnership. This rule is especially applicable where the business, or a part of it, to be carried on by the partnership is *ultra vires* in respect to the corporation entering into such a relation.

Corporations have the full power, when acting in furtherance of their proper corporate objects, to the same extent as natural persons to act as an agent or attorney, and to employ others in the management and conduct of their business. They also have the full power to bring all necessary actions and proceedings for the enforcement of their rights or the protection of their property, and the possession of this power to sue necessarily implies the lesser one of compromising and adjusting differences which may arise in connection with the conduct of their corporate business.

§ 70. **Power to Acquire Stock in Other Corporations.** This power, necessarily, must be expressly conferred. Corporations have no legal right to purchase and hold the stock of other corporations, for otherwise it would be possible for them to substantially engage in a business not authorized by their charter. This condition might subject the stockholders to risks not intended to be assumed by them, and the State, further, might be deprived of its right to control and to regulate the integral business of the corporation. In many cases, the right is directly conferred in the charter, but even where the power is expressly conferred it is limited to the acquisition of capital stock in corporations organized for the same general purposes and objects as the holding company.

§ 71. **Power in Respect to Consolidation.** This power is also one which must be expressly conferred by the charter

of a corporation used in its broad sense. No implied power exists in a corporation to consolidate with others, even with those organized for the same general purposes. Public policy is the basis of this principle. If consolidations were permitted without restraint, especially by corporations of a quasi-public nature, the healthful competition necessary to the best welfare of the community might be seriously impaired or entirely destroyed. In many States, statutes have been passed prohibiting the acquirement or the consolidation, under any circumstances, of parallel and competing lines of railway.

Methods and Meaning of Consolidation. By consolidation is understood a merging or amalgamation of two or more corporations into one corporate body whereby their powers, properties, and privileges, together with their liabilities and obligations, pass to and devolve upon a new juridical person. The resulting extent of the powers to be exercised and the liabilities to be assumed by the new corporation will depend, necessarily, upon the terms of the legislative consent authorizing the consolidation.

Several methods of consolidation are adopted, one of which may result in the merging of two or more corporations, one remaining in existence and taking to itself all of the rights, properties, franchises, and duties of the others, which are dissolved; the merging of two or more corporations into a new one, the consolidation resulting in the dissolution of the old corporations and the new one acquiring the right to possess, enjoy, and assume all of the rights, duties, properties, and liabilities of the companies dissolved; or the combination of several companies, all of which remain in existence, but which are controlled by one set of managing officers or directors. A private corporation is a purely voluntary corporation, and it is without the power of the State to force a group of persons to organize and exercise or possess corporate capacities. Equally so a consolidation in any of its forms cannot be forced upon independent and separate corporations. The act is a purely voluntary one on their part under the grant of legis-

lative authority to each of the constituent companies. At common-law, corporations have no implied power to consolidate or to form partnerships, and the rule obtains in this country that the corporation can only exercise those powers authorized by its charter. The consent of the State must be expressly conferred, and the absence of prohibition will not be construed as an implied consent on its part.

Consent of the Stockholder. The charter of the corporation is a contract, not only between the State and the corporation, but also between its members, and this original contract cannot be altered without their consent. The rule, therefore, necessarily follows that unless consolidation statutes provide for the consent of a stated majority to the consolidation, the consent of every stockholder is necessary. Where a corporation is organized under the general laws which permit its consolidation, the implied consent of the stockholders is presumed, as the power to consolidate constitutes a part of the contract between the stockholders; and a stockholder may be also estopped to contest a consolidation by his own acts, or his rights in this respect may be lost by his laches.

The property rights of stockholders, however, are not affected by the legality of the consolidation, as they cannot be forced into a consolidated company against their consent. If a majority, or a required statutory proportion, determine upon consolidation, the rule generally obtains that a dissenting stockholder cannot prevent action of this character by the corporation. He cannot be, however, deprived of his property or rights in the corporation, and provision is usually made securing these to the stockholders who refuse to come in.

Rights of Creditors on Consolidation. The liabilities of the constituent companies usually are assumed by the consolidated company; or, in some cases, where the constituent companies are not dissolved, their liabilities can be enforced only against them or against their property taken over by the new and consolidated corporation. Generally, when corporations are consolidated, the new company takes

the properties, rights, and franchises of the old corporations subject to the same liabilities and burdens which attach to the charter and business of the constituent companies.

"For the purpose of answering for the liabilities of the constituent corporations, the consolidated company should be deemed to be merely the same as each of its constituents, their existence continued in it under the new form and name, their liabilities still existing as before and capable of enforcement against the new company in the same way as if no change had occurred in its organization or name." [24] Where the old companies are dissolved upon consolidation, the rights of creditors continue in force against the consolidated company in equity against the assets of the constituent companies in the hands of the consolidated company. Creditors have no right to prevent a consolidation or combination of corporations, but they cannot, by this action, be deprived of any of their rights or remedies against the constituent companies.

[24] Indianapolis, etc., Ry. Co. v. Jones, 29 Ind. 465.

CHAPTER VIII

ULTRA VIRES ACTS

§ 72. Definition and Discussion of Doctrine. The term *ultra vires* is used to express the action of a corporation in excess of or beyond the powers conferred, either expressly or impliedly, upon it by its charter. The existence of a legal right or cause of action as resulting from the *ultra vires* act is the essential question involved. There are two doctrines followed by the courts, one, known as the strict rule or doctrine of *ultra vires,* viz, that all acts of the corporation not within the powers conferred upon it or reasonably implied from its charter are absolutely null and void. The other rule or doctrine is known as the liberal one, and this holds that *ultra vires* acts, so far as their legal effect is concerned, are not absolutely null and void, but merely voidable. When an *ultra vires* act is spoken of as beyond the powers of the corporation, it must be remembered that the word power is used in the sense of legal authority or right and not of mere capacity. In this sense a corporation has no power to perform any act which is outside or in excess of the authority conferred upon it or reasonably implied from its charter, but, like a natural person, it has the capacity or the ability to perform many acts which are unauthorized, some of which may be actually wrongful or positively criminal. A natural person may be prohibited by law from committing the crime of murder. The act is in excess of or beyond his lawful powers, but the prohibition does not prevent the commission of many crimes of this nature.

As illustrative of this idea, a New York case can be read with interest and profit, where Chief Justice Comstock said:

"But such, I apprehend, is not the nature of these bodies; like natural persons, they can overleap the legal and moral restraints imposed upon them: In other words, they are

capable of doing wrong. To say that a corporation has no right to do unauthorized acts, is only to put forth a very plain truism; but to say that such bodies have no power or capacity to err, is to impute to them an excellence which does not belong to any created existences with which we are acquainted. The distinction between power and right is no more to be lost sight of in respect to artificial than in respect to natural persons. . . . One of the sources of error, in reasoning upon legal as well as other questions, is exactness in the use of language, or perhaps in the imperfectness of language to express the varieties of thought. It is a self-evident truth, that a natural person cannot exceed the powers which belong to his nature. In this proposition, we use words in their literal and exact sense. In the same sense, it is a truth, equally evident, that a corporation cannot exceed its powers; but this is only asserting that it cannot exercise attributes which it does not possess. As an impersonal being, it cannot experience religious emotion, nor feel the moral sentiments. Corporations are said to be clothed with certain powers enumerated in their charters or incidental to those which are enumerated, and it is also said, they cannot exceed those powers; therefore it has been urged, that all attempts to do so are simply nugatory. The premises are correct, when properly understood; but the conclusion is false, because the premises are misinterpreted. When we speak of the powers of a corporation, the term only expresses the privileges and franchises which are bestowed in the charter; and when we say it cannot exercise other powers, the just meaning of the language is, that as the attempt to do so is without authority of law, the performance of unauthorized acts is a usurpation, which may be a wrong to the State, or, perhaps, to the shareholders. But the usurpation is possible. In the same sense natural persons are under the restraints of law, but they may transgress the law, and when they do so, they are responsible for their acts. From this consequence, corporations are not, in my judgment, wholly exempt."[1]

An *ultra vires* act is not necessarily regarded as not being in all cases the act of the corporation. Where real property has been acquired contrary to law by it, the general rule obtains that the title passes none the less. A

[1] Bissell v. Michigan Southern R. R. Co., etc., 22 N. Y. 259.

corporation may commit an offense contrary to express statutory provision for which it may be punished. A contract in excess of the powers of a corporation may be made by it, but this may still be enforced under the liberal rule relating to *ultra vires* acts.

§ 73. Misapplication of Term (Ultra Vires). In this connection the doctrine of special and general capacities of a corporation, as discussed in section 52, should be referred to. It is not necessary to repeat it here. The decisions upon the subject of *ultra vires* are many, confusing, and conflicting. No general rule can be stated which will be of assistance in positively and definitely determining the answer to the essential question, viz, the legal rights following or resulting from the doing of an *ultra vires* act by a corporation. It will be found upon investigation that in many cases the decision turns upon the parties complaining, whether the State, taking cognizance of a violation of its prohibitions or grants, or private persons engaged in litigation over a business transaction in which no other parties may be interested except themselves. The decision, again, may depend upon the person against whom the relief is sought in the proceeding which involves the legal effect of the *ultra vires* act; and, again, the decision may turn upon the relief sought, whether a forfeiture of the charter of the corporation, the enforcement of a contract, or the enforcement of their rights claimed to exist by reason of the act done in excess of the corporate powers.

The confusion in the authorities upon this whole general topic is manifest from an examination of them, and much of it has arisen from a misapprehension of the true limits and application of the doctrine of *ultra vires*. Cases are to be found where acts which require the consent of the stockholders to make them binding have been done without such consent, and these are spoken of as *ultra vires* acts, when in truth they are mere violations of the general law of agency. Such acts might be beyond the powers of the managing officers of the corporation, but would not be beyond or in excess of the powers of the corporation itself.

Again, cases are to be found in which directory provisions of the charter have prescribed that certain acts shall be done in a certain manner and these acts have been performed without observing the required formalities. These have been referred to as *ultra vires* acts, when it is apparent that in the absence of any intention on the part of the legislature to make such provisions mandatory or to impose penalties for their non-observance, they are mere irregularities and do not seriously affect the transaction. There are also acts which are forbidden by statute or common law, or against good morals or public policy which are classed as *ultra vires* acts. The better authorities treat these cases as governed by the same principles of law controlling an individual and hold the act or contract unenforcible, not because it is *ultra vires* merely, but because it is positively unlawful.

§ 74. Classes of Ultra Vires Acts. To clarify the subject as much as possible, acts stated to be *ultra vires* by the authorities may be classified into acts in excess of the corporate powers, as conferred by the charter of the corporation expressly, or by reasonable implication. To this class alone, in the proper sense of the term *ultra vires,* can this character be properly ascribed. Another class of acts termed *ultra vires* by some authorities, but which are not in the strict sense of the word, are those where the corporation is authorized to exercise powers by and through the consent of the stockholders, but which the corporation has done without this consent. Corporations may be also authorized to exercise certain powers for designated purposes. The power is, however, exercised for a different purpose or in excess of the designated power. There is clearly here a distinction between a want of power and a misuse of power. And, finally, there are also corporate acts which are valid if done in a certain manner by the corporation, but otherwise not. Here there is a clear distinction between a want of power and a lack of necessary formality in the execution of that power. Using the term *ultra vires* in its proper sense, acts of the last three classes

named cannot be regarded as coming within the term, although many authorities regard some or all of them of this character.

These distinctions have been made, however, in many cases, where the true concept of the term *ultra vires* is understood by the court. In a New Jersey case, Camden etc. Ry. v. May's Landing, 48 N. J. L. 530, in a dissenting opinion, but none the less valuable on this point, it was said:

"The indiscriminate use of this expression with respect to cases different in their nature and principles, has led to considerable confusion if not misapprehension. Where an act done by directors or officers is simply beyond the powers of the executive department of the corporation, the agency by which the corporation organizes its functions, and not of the corporation itself, it may be made valid and binding by the action of the board of directors or by the approval of the stockholders. Where the act done by the directors is not in excess of the powers of the corporation itself, but is simply an infringement upon the rights of other stockholders, it may be made binding upon the latter by ratification, or by consent implied by acquiescence. Where the infirmity of the act does not consist in a want of corporate power to do it, but in the disregard of formalities prescribed, it may or may not be valid as to third persons dealing *bona fide* with the corporation, according to the nature of the formalities not observed or the consequences the legislature has imposed upon non-observance. These are all cases depending upon legal principles not peculiarly applicable to corporations, and the use of the phrase *ultra vires* tends to confusion and misapprehension. In its legitimate use, the expression *ultra vires* should be applied only to such acts as are beyond the powers of the corporation itself."

§ 75. The Strict Rule and Its Reasons. The strict rule of *ultra vires* has already been briefly stated. The rights of different parties may be involved in the act. The act may be one in violation of the terms of its charter and where the State elects to take cognizance of it and punish the corporation for the use of powers not granted. The

right of the State to proceed against the corporation in these cases is plain. The rights of innocent third parties may be and are frequently also involved in the same transaction, and an effort to render substantial justice to the individual, and at the same time follow with logical consistency the rule that a corporation can exercise only those powers conferred upon it by its charter directly or by reasonable implication, leads to hopeless confusion in the cases. The strict rule of *ultra vires,* viz, that no legal results follow from the doing of the act of the corporation in excess of its powers, is followed with more strictness by the English cases and the Federal courts in this country than in many other jurisdictions. Thompson on Corporations, applying the rule to contracts, states it as follows:

"A contract of a corporation which is either unauthorized by or in violation of its charter or governing statutes, or which is entirely outside the scope of the powers of its creation, is void in the sense of being no contract at all, because of the want of power in the corporation to enter into it. That such a contract will not be enforced by any species of action in a court of justice, that being void *ab initio* (from the beginning), it cannot be made good by ratification or by any succession of renewals, and that no performance on either side can give validity to it so as to give a party to the contract any right of action upon it."[2]

The reasons upon which the strict rule of *ultra vires* rests were concisely and clearly stated by Justice Gray in a case in the Supreme Court of the United States:[3]

"The reason why a corporation is not liable upon a contract *ultra vires,* that is to say, beyond the powers conferred upon it by the legislature, and varying from the objects of its creation, as declared in the law of its organization, are: (1) The interest of the public that the corporation shall not transcend the powers granted; (2) The interest of the stockholders that the capital shall not be subjected to the risk of enterprises not contemplated by the

[2] Thompson on Private Corporations, § 5355.

[3] Pittsburgh, etc., R. R. Co. v. Keokuk, etc., Bridge Co., 131 U. S. 371.

charter, and therefore not authorized by the stockholders in subscribing for stock; (3) The obligation of everyone entering into a contract with a corporation to take notice of the legal limits of its powers."

And in an Iowa case, Lucas v. White Line, etc. Co., 70 Iowa, 541, the court said, referring to the strict rule and some modifications:

"Corporations and officers do not always keep within their powers, and the application of the doctrine of *ultra vires* is often attended with very perplexing questions. By the application of a few plain rules, however, we may readily reach the proper answer to the questions involved in the case: (1) Every person dealing with a corporation is charged with knowledge of its powers as set out in its recorded articles of incorporation; (2) Where a corporation exercises power not given by its charter it violates the law of its organization, and may be proceeded against by the State through its attorney-general, as provided by the statute, and the unanimous consent of all the stockholders can not make illegal acts valid. The State has the right to interfere in such cases; (3) Where a third party makes with the officers of a corporation an illegal contract beyond the powers of a corporation, as shown by its charter, such third party can not recover; because he acts with knowledge that the officers have exceeded their powers, and between him and the corporation or its stockholders no amount of ratification by those unauthorized to make the contract will make it valid; (4) Where the officers of a corporation make a contract with third parties in regard to matters apparently within their corporate powers, but which, upon the proof of extrinsic facts of which the parties had no notice, lie beyond their powers, the corporation must be held, unless it may avoid liability by taking timely steps to prevent loss or damage to such third parties; for in such cases the third party is innocent, and the corporation or stockholders less innocent for having selected officers not worthy of the trust reposed in them."

§ 76. The Liberal Rule. Under the operation of the strict rule commonly followed by the English and Federal courts, an *ultra vires* act is treated as a nullity. On the other hand, a great many authorities in the States, while

acquiescing in the general doctrine that the corporation cannot act as a matter of theory in excess of its powers, and conceding that an *ultra vires* contract as such cannot be enforced, adhere to the view that it is not a nullity, but merely voidable and may be the basis of an estoppel by direct act or acquiescence; or they proceed upon the general doctrine that while they will not lend their aid to further promote or enforce an *ultra vires* transaction, they will not permit a party who has obtained a benefit thereby to interpose *ultra vires* as a defense. In other words, they attempt to do substantial justice, even though in so doing they may indirectly enforce an *ultra vires* act. Stated concisely, this doctrine may be summed up in a definition of the liberal rule, that an *ultra vires* act is not void but merely voidable when the application of the strict rule would not advance justice, but, on the contrary, would accomplish a legal wrong. It might be said, in connection with a discussion of the two rules, that the strict rule is applied to public corporations in all its severity, and its original use in respect to private corporations by the English decisions followed from its existence and its application against corporations of the character noted. For equitable reasons, it would appear that the liberal rule is the one to be applied in all cases involving private corporations. In the transaction of business by a public corporation, the interests of the public from the corporate standpoint alone are involved. Private corporations, on the other hand, are private enterprises employing personal and private capital, and only in exceptional cases involving, in the conduct of their business, the interests of the public.

§ 77. Effect of Ultra Vires Contracts. It is impossible to lay down any general rules regarding the enforcibility of *ultra vires* contracts which would apply in all cases or be recognized in all courts. Where the liberal *ultra vires* rule is followed, the facts of a particular case determine the rights and equities of the parties, and even in those courts where the strict rule controls, decisions are rendered which modify materially its application. The general

results of all of the authorities may be summed up substantially in the following general propositions classified, as will be noted, upon the extent to which the *ultra vires* act has proceeded.

Executed on Both Sides. Where an *ultra vires* contract has been entered into and fully performed on both sides, the courts, without exception, hold that neither party can maintain an action to set aside the transaction or to recover the consideration that has been paid. The parties will be left in *statu quo*, and this rule is followed in those jurisdictions in which the strict doctrine of *ultra vires* is followed as well as in those jurisdictions where the contrary holding prevails. "The executed dealings of corporations must be allowed to stand for and against both parties when the plainest rules of good faith so require."[4]

Executory on Both Sides. An *ultra vires* contract executory on both sides is void and cannot be enforced in any jurisdiction, for courts will not lend their assistance to enforce a void contract. This rule applies, however, only to those contracts which are clearly *ultra vires*. Where it is within the apparent scope of the corporate powers and *ultra vires* because of outside facts peculiarly within the knowledge of the corporation and without the knowledge of the other party to the transaction, the courts have frequently held the corporation estopped to deny its power to enter into a particular contract.

Partially Executed. If the *ultra vires* contract has been executed wholly or partially by both or one of the parties, the weight of authority in the State courts is to the effect that the party receiving benefits is estopped to assert the claim that the corporation had no authority to make the contract; and while the contract itself may not be directly enforced, the one who has, in good faith, parted with value or suffered damage in reliance upon it, will not be estopped to obtain relief by recovering what he has parted with or its value. In the jurisdictions where the strict rule of *ultra vires* obtains, it is held that under the circumstances

[4] Parish v. Wheeler, 22 N. Y. 494.

noted above, while the contract itself will not be enforced because the corporation was incapable of making it, yet the one parting with an advantage or property will be permitted to recover in an action quasi *ex-contractu* the money paid or loaned or the value of the property delivered or services rendered under and pursuant to the contract. In a leading case in the Supreme Court of the United States,[5] the court reiterated its uniform holding of the strict rule of *ultra vires,* and held that the contract between the two corporations, in order to bind either of them, must be within the corporate powers of both. That a contract beyond the powers conferred upon a corporation by the legislature is not voidable only, but wholly void. It cannot be ratified by either party. No performance on either side can give the unlawful contract any validity nor be the foundation of any right of action upon it. And, further, that neither the corporation nor the other parties to the contract can be estopped by assent to it or by acting upon it to show that it was prohibited. But the court, in the course of its decision, after reviewing many authorities, said:

"A contract *ultra vires* being unlawful and void, not because it is in itself immoral, but because the corporation by the law of its creation is incapable of making it, the courts, while refusing to maintain any action upon the unlawful contract have always striven to do justice between the parties so far as it could be done consistently with adherence to law by permitting property or money parted with on the faith of the unlawful contract, to be recovered back, or compensation to be made for it. In such case, however, the action is not maintained upon the unlawful contract, nor according to its terms; but on an implied contract of the defendant to return, or failing to do that, to make compensation for, property or money which it has no right to retain. To maintain such an action is not to affirm, but to disaffirm, the unlawful contract."

And in an earlier case, Salt Lake v. Hollister (118 U. S. 256), the same court stated that

[5] Central Transportation Company v. Pullman Palace Car Co., 139 U. S. 24.

"In cases of contracts upon which corporations could not be sued because they were *ultra vires*, the courts have gone a long way to enable parties who had parted with property or money on the faith of such contracts to obtain justice by the recovery of the property or the money specifically or as money had and received to the plaintiff's use."

Many cases will be found referred to in the Central Transportation Company case above cited and upholding the equitable doctrine there stated.

The State courts also generally hold that there exists an obligation, even where the corporation repudiates an *ultra vires* act, to restore what it has received under the contract, and the same is true of the other party to it. "However the contractual power of the corporation may be limited under its charter, there is no limitation of its power to make restitution to the other party whose money or property it has obtained through an unauthorized contract; nor, as a corporation, is it exempt from the common obligation to do justice which binds individuals, for this duty rests upon all persons alike, whether natural or artificial."[6]

If a corporation obtains money through an *ultra vires* act and uses this money to pay existing and valid indebtedness, the person from whom the money was obtained is deemed in equity to be subrogated to the rights of the creditors of the corporation whose claims were paid thereby.

Retention of Benefits; Estoppel. In holding that an *ultra vires* contract can be enforced, the courts following the liberal rule of *ultra vires* generally base their decision upon the fact that by reason of part performance one or the other of the parties has received and retains benefits under the contract, and that so long as the benefits are retained no claim can be made that one or both of the parties had no power to make the contract. Chief Justice Gilfillan, in a Minnesota case, said:

"There are few rules better settled or more strongly supported by authority with fewer exceptions in this country,

[6] The Manchester, etc., R. R. Co. v. Concord R. Co., 66 New Hamp. 100.

that when a contract by a private corporation, which is otherwise unobjectionable, has been performed on one side, the party that has received and retains the benefit of such performance, shall not be permitted to evade performance on the ground that the contract was in excess of the purposes for which the company was created. The rule may not be strictly logical but it prevents a good deal of injustice.'"[7]

And in a late Wisconsin case, Lewis v. American etc. Association, 98 Wis., 203, the court said:

"It is well settled that a corporation cannot avail itself of the defense of *ultra vires* when the contract in question has been in good faith fully performed by the other party and the corporation has had the full benefit of the performance of the contract. Much less will the claim that the transaction was *ultra vires* be allowed as a ground for rescinding the contract and restoring to the complaining party on that ground the property or funds with which he has parted after he has had the benefit of full performance of the contract by the other party; and, in general, the plea of *ultra vires* will not be allowed to prevail, whether interposed for or against a corporation when it will not advance justice but, on the contrary, will accomplish a legal wrong."

§ 78. Acquiescence in and Ratification of Ultra Vires Acts. To entitle a stockholder to relief against the results of the *ultra vires* acts by a corporation, he must act promptly or he will be bound by his laches. Corporate members may restrain, in the proper proceedings, *ultra vires* acts when still executory; but relief will not be granted in the majority of jurisdictions when the acts complained of have been either wholly or partially executed on one or both sides, unless some great public interest is involved.

§ 79. Rule as to Negotiable Paper. In this country private corporations organized for pecuniary purposes have the implied power, unless prohibited by their charters, to execute negotiable instruments when within their proper

[7] Seymour v. Guaranty, etc., Society, 54 Minn. 147.

corporate purposes. If negotiable paper is issued in excess of their authorized powers as between the original parties, it will be void when the transaction was affected by notice of its *ultra vires* character. An innocent purchaser for value is usually protected, however, as he has a right to presume that the paper was made or endorsed in the usual course of business and was binding upon the corporation. A different rule obtains, however, where an express statutory provision prohibits the issue of negotiable paper.

§ 80. Result of Ultra Vires Acts. Where a corporation does an *ultra vires* act or one in excess of and beyond its charter powers, it clearly has violated an express or implied prohibition of the State creating it and granting or withholding corporate powers and capacities. The State unquestionably has the right to maintain proceedings for the forfeiture of that charter and the dissolution of the corporation. This right belongs, however, to the State alone, as a corporation derives none of its powers from third parties, even those which may be involved in the *ultra vires* act. A forfeiture of the charter of the corporation deprives it of its legal existence. It is the equivalent of capital punishment in the case of a natural person. It is only in unusual cases and those where there has been a persistent and defiant violation of charter provisions that this extreme punishment is sought even by the State to be inflicted upon the offender. The rule was well stated in a case brought under the New York laws for a violation of statutes relative to the organization and conduct of trusts.[8] The court here said:

"To justify forfeiture of corporate existence a State as prosecutor must show, on the part of the corporation accused, some sin against the law of its being which has produced or tends to produce injury to the public. A transgression must not be merely formal or incidental, but material and serious and such as to harm or menace the public welfare; for the State does not and should not concern itself with the quarrels of private litigants. It furnishes for them

[8] People v. North River Sugar Refining Co., 121 N. Y. 582.

sufficient courts and remedies, but intervenes as a party only when some public interest requires its action."

And in a Minnesota case,[9] the court said:

"Courts always proceed with great caution in declaring a forfeiture of franchises, and require the prosecutor seeking the forfeiture to bring the case clearly within the rules entitling him to exact so severe a penalty. . . . Hence, if they engage in any business not authorized by the statute, it is *ultra vires,* or in excess of their powers, but not a usurpation of franchises not granted, nor necessarily a misuser of those granted. Acts in excess of power may undoubtedly be carried so far as to amount to a misuser of the franchise to be a corporation and a ground for its forfeiture. How far it must go to amount to this the courts have wisely never attempted to define, except in very general terms, preferring the safer course of adopting a gradual process of judicial inclusion and exclusion as the cases arise. But we think it may be safely stated as the general consensus of the authorities that, to constitute a misuser of the corporate franchise, such as to warrant its forfeiture, the *ultra vires* acts must be so substantial and continued as to amount to a clear violation of the condition upon which the franchise was granted, and so derange or destroy the business of the corporation that it no longer fulfills the end for which it was created. But, in case of excess of powers, it is only where some public mischief is done or threatened that the State, by the attorney-general, should interfere. If, as between the company and its stockholders, there is a wrongful application of the capital, or an illegal incurring of liabilities, it is for the stockholders to complain. If the company is entering into contracts *ultra vires,* to the prejudice of persons outside the corporation, such as creditors, it is for such persons to take steps to protect their interests. The mere fact that acts are *ultra vires* is not necessarily a ground for interference by the State, especially by *quo warranto* to forfeit the corporate franchises. It should also be borne in mind that acts *ultra vires* may justify interference on the part of the State by injunction to prohibit a continuance of the excess of powers which would not be sufficient ground for a forfeiture in proceedings in *quo warranto.*"

[9] State v. Minnesota Thresher Mfg. Co., 40 Minn. 213.

CHAPTER IX

LIABILITY FOR TORTS AND CRIMES

§ 81. Common-Law Conception of Corporation. The common-law conception of a corporation was that of an artificial person, invisible and intangible, with neither soul nor body and with no moral sense. Legally capable of exercising only the powers conferred, its capacity to commit either torts or crimes was necessarily denied. It was repeatedly adjudged that they could not be subjected in actions of trover, trespass, or disseizin; that they could not commit crimes nor be liable for torts, with few exceptions. The old idea of a corporation without a soul is more quaint than substantial, and the theory of the doctrine that a corporation, by its charter, could exercise only those powers beneficial in themselves is contrary to the modern and the common-sense idea, that if it is possible for a corporation to act from good motives, it can also act upon bad ones. They can intend to do evil as well as to do good. This is substantially the modern doctrine through the application of which corporations are held liable for their torts and subject to punishment for the commission of many criminal offenses. The law of private corporations, within the last half century, has been in progress of development, and has grown up from a few rules and maxims into a substantial body of law. Corporations have so multiplied and extended that they are connected with and in a great degree influence all the business transactions of the country and give character to some extent to society itself. Corporations, instead of being the soulless and unconscious beings of Lord Coke's times are the great motive powers of society, governing, regulating, and transacting its chief business affairs. They act not only upon pecuniary concerns, but as having conscience and motives, and to an almost unlimited extent they are entrusted with the benevolent and religious agencies

of the day and are constituted trustees and managers of large funds promotive of such objects.

§ 82. **Liability for Torts.** The development of the law respecting private corporations, in respect to the subject of this chapter, has progressed with its development along other lines, and it is now the settled rule that a corporation is liable in civil action for torts committed by its agents and servants the same as a natural person. When a corporate officer or agent acts within the apparent scope of his power or authority, the corporation is bound by his acts, and is liable to third parties who may have sustained damages by reason of them. For the unauthorized and unlawful tortious acts of its officers and agents, it is only liable when the corporation has subsequently ratified or adopted them. To create a liability for an unauthorized and unlawful act of the corporate officers and agents, it must appear that they were expressly directed to do the act, or that it was done in pursuance of general authority relative to the subject of it. Where the act is within the scope of the general powers of the corporation, its liability is not defeated by the fact that the corporate agents have assumed to do and have done that which the corporation itself could not rightfully do. A corporation may do wrong through its agents and be subjected to a liability for the consequences of that wrongful act. The modern doctrine holds that the liability extends to torts, involving a specific intent or the element of malice, as libel, fraud, malicious prosecution, or conspiracy.

Damages Recoverable. The commission of a tort may lead to the recovery of punitive damages by the one injured. It is now held that a corporation may be liable in punitive damages under the same circumstances as a natural person acting through an agent would be held. The decisions, however, are conflicting on the question of punitive damages, and some still hold that only actual damages can be recovered; others, that punitive damages will be allowed when the wrongful act of the agent was willful and intentional; and still others hold that punitive damages can

be recovered only when the wrongful act was done under the express direction of the corporation or afterwards ratified by it.

Motive and Intent as Elements. For many years the decisions made a distinction in determining the liability of the corporation for its acts or conduct, between those for which the actor is liable, independently of motive and which are injurious, and those the nature or character of which depends upon the motive, and which, apart from this, cannot be made a ground of liability. Many authorities have maintained that because a corporation was incapable of possessing motives or evidencing an intent, where the act involved these as an essential ground of recovery, that the corporation could not be held. The tendency of modern decisions is to ignore the distinctions as to corporations and to apply the same principles which are applied to natural persons acting under similar conditions. An early case in Connecticut is illustrative of this modern tendency.[9] This was an action based on the provisions of the Connecticut statutes entitled "An Act to Prevent Vexatious Suits", and the court held that it was subjected to the same general principles as actions in a case for malicious prosecution at common law. The plaintiff alleged that the defendant, a corporation, without probable cause, with malicious intent, unjustly to vex, harass, embarrass, and trouble the plaintiff, had commenced, by writ of attachment, and prosecuted against him, a certain vexatious suit and action for fraudulent representations, to the injury of the bank. There was a motion for non-suit which was granted by the lower court but which was set aside on appeal. The question involved in this case was whether a corporation could act from malice, and therefore commence and prosecute a malicious or vexatious suit. This was decided in the affirmative by the appellate court, where this language was used:

"But after all, the objection to the remedy of this plaintiff against the bank in its corporate capacity is not so much

[9] Goodspeed v. Bank, 22 Conn. 530.

that as a corporation it cannot be made responsible for torts committed by its directors, as that it cannot be subjected to that species of tort which essentially consists in motive and intention. The claim is, that, as a corporation is ideal only, it cannot act from malice, and, therefore, cannot commence and prosecute a malicious or vexatious suit. This syllogism, or reasoning, might have been very satisfactory to the schoolmen of former days; more so, we think, than to the jurist who seeks to discover a reasonable and appropriate remedy for every wrong. To say that a corporation cannot have motives, and act from motives, is to deny the evidence of our senses, when we see them thus acting, and effecting thereby results of the greatest importance, every day. And if they can have any motive, they can have a bad one; they can intend to do evil as well as to do good. If the act done is a corporate one, so must the motive and intention be."

As illustrating the tendency and holdings of courts on the questions suggested above, a few quotations will be instructive:

"A corporation is liable to the same extent and under the same conditions as a natural person for the consequences of its wrongful acts and will be held to respond in a civil action at the suit of an injured party for every grade and description of forcible, malicious, or negligent tort or wrong which it commits, however foreign to its nature or beyond its granted powers the wrongful transaction or act may be."[10]

"Corporations are liable for every wrong they commit, and in such cases the doctrine of *ultra vires* has no application. They are liable for the acts of their servants while such servants are engaged in the business of their principal in the same manner and to the same extent that individuals are liable under like circumstances. An action may be maintained against a corporation for its malicious or negligent tort, however foreign they may be to the object of its creation or beyond its granted powers. It may be sued for assault and battery, for fraud and deceit, for false imprisonment, for malicious prosecution, for nuisance and for libel."[11]

[10] New York, etc., R. R. Co. v. Schuyler, 34 N. Y. 30.

[11] National Bank v. Graham, 100 U. S. 699.

§ 83. Commission of Crime. In general, a corporation may be responsible for omissions to perform specific duties imposed by law. They are subject to punishment for some acts of misfeasance, but not ordinarily for crimes which involve a mental operation or the element of personal violence. There are also some crimes which a corporation, from its intangible nature, can not commit. A corporation may also be guilty of contempt of court and punished the same as a natural person. Bishop on Criminal Law, Sec. 417, states their liability as follows:

"A corporation cannot, in its corporate capacity, commit a crime by an act in the fullest sense *ultra vires* and contrary to its nature but within the sphere of its corporate capacity and to an undefined extent beyond. Whenever it assumes to act as a corporation it has the same capabilities of criminal intent and of act, in other words, of crime, as an individual must sustain to the thing of like relation."

There exists at the present time no distinction between the acts of misfeasance and of nonfeasance, at least where no criminal intent is involved.

The crimes involving criminal intent, and which from their nature a corporation is incapable of doing, are, among others, murder, larceny, and assault and battery, although a corporation may be liable civilly for punitive damages caused by an assault and battery, or a malicious prosecution and other torts involving intent. In keeping with these rules of liability, a corporation has been held subject to indictment for criminal libel, for keeping a disorderly house, obstructing navigation, for committing a public nuisance, for Sabbath breaking, and for usury.

CHAPTER X

MEMBERSHIP IN CORPORATIONS

§ 84. General Statement. The division of corporations into stock and non-stock will be considered for the purposes of this chapter. A stock corporation is one having shares of capital stock of the par value and to the amount designated in its charter. A non-stock corporation is one having no capital stock. The former are usually organized for the purpose of the pecuniary gain and advantage of its members. The latter are usually formed for the purpose of advancing and promoting, in behalf of its members and others, other objects than the financial benefit or advantage of its members. The methods of acquiring membership and the loss of that membership when acquired are essentially different in the two classes of corporations.

§ 85. Non-Stock Corporations. The charter, or the by-laws, of a non-stock corporation, determines the method by which membership must be acquired. Admission of members is usually under the absolute control of the corporation, subject to restrictions, if any, found in the laws of the State or in the articles of incorporation. Persons may become members either by joining in the original organization of the corporation, or, subsequently, upon being admitted to membership in accordance with its regulations, usually consisting of the requirements of an application for membership and a vote of approval by existing members. Membership in a non-stock corporation, it will be seen, is determined, not by the ownership of an interest in the corporation, or even the possession of the required qualifications, but upon the approval by the members of an existing corporation to admit to membership.

§ 86. Stock Corporations. Membership in a corporation having shares of capital stock is acquired through the

ownership of one or more of the aliquot parts into which the capital stock of the corporation is divided. The personal approval of the existing members of a corporation is not necessary nor the possession of any personal qualification. If an individual becomes the owner, in any legitimate way, of one or more of the aliquot shares into which the capital stock is divided, he thereby becomes a member of the corporation, although his personality may be distasteful or obnoxious to every other member of that corporation. He is a member in the full legal sense of the word and entitled to all of the rights which attach to the ownership by him of his proportionate part of the capital stock of the corporation. His interest in the corporation is evidenced, usually, by what is termed a certificate of stock, though its issue by the corporation and possession by the member is not necessary to constitute that relation. It is the ownership of an interest in the capital stock of the corporation that constitutes one a member. His name may appear on the books of the company as the owner of an interest, but this does not necessarily establish the relation. This subject will be discussed later in the chapter on capital stock. One may become an owner of the capital stock of a corporation by acquiring it through purchase or devise, by subscription to the shares of stock of the corporation, and through the operation of the doctrine of estoppel. The latter rule is applied where one, without owning shares of stock in a corporation, assumes the rights of membership and acts in accordance with that relation; holding himself out, in other words, to the public dealing with the corporation and with himself as a member of that corporation. The courts hold, where this condition exists, that in subsequent controversies or litigation arising from these acts, he will be estopped to assert his non-membership.

§ 87. Who Can Be Members. The relation existing between a corporation, the State, and its members, and between its members, is a contract one, and it follows that in the absence of statutory provisions only those who are capable of entering into a contract relation may become

members of a stock corporation. Infants may, however, acquire stock in a corporation, but this particular contract will be entered into subject to the principles of law controlling, in general, the contracts of those *non sui juris*. The right of affirmance or disaffirmance will exist upon attaining majority. The authorities are agreed that if an infant accepts the benefits of membership in a stock corporation he is also responsible for the liabilities following that relation and subject, therefore, to calls and assessments. Where the common law disability relating to married women prevails they are, even if of legal age, subject to the controlling principles of the law limiting their capacity to enter into contracts. In nearly all States, however, "Married Women Acts", so-called, have been passed removing the common-law disability, and in these States they are free, if of age, to enter into this particular contract relation as freely as other persons *sui juris*. They can become shareholders in stock corporations, entitled to the benefits and subject to the liabilities created through the existence of the relation. The right of one corporation to become a member of another stock corporation has already been discussed. The general rule may be repeated here, viz, that the legal right does not exist unless expressly conferred, the doctrine applying both to the acquisition of shares in another corporation as well as shares of its own stock. Trustees and others occupying a trust relation may become members of a stock corporation for the benefit of their *cestui que trust*. Statutory provisions exist in many States declaring the trustee under such circumstances to be merely a nominal legal owner of the shares, the trust estate constituting the true owner and in their absence this rule will still obtain.

§ 88. **Loss of Membership.** Membership in a stock corporation is lost by the transfer of the interest owned by the member to another. Membership in a non-stock corporation is lost by death, resignation or through expulsion, a resignation being the voluntary relinquishment or membership in a corporation, while expulsion is an involuntary,

loss of membership. In non-stock corporations the power of expulsion is determined by the constitution and by-laws of the association or the corporation, and the member must give his assent to by-laws regulating expulsion before they can become operative upon him, though acceptance of membership with knowledge of the by-laws is usually held by the courts to constitute an implied assent.

§ 89. **Requisites to Legal Expulsion.** An individual possesses both personal and property rights. The former including with others, life, liberty, health, and reputation. These personal rights are regarded by the courts as entitled to protection, and both the Federal and State constitutions abound in provisions insuring to the individual the possession and enjoyment of his fundamental personal rights. Expulsion from a non-stock corporation may seriously affect or entirely destroy one of the most desirable and important of personal rights, viz, that of reputation. The courts, therefore, have universally held that before a member can be expelled from a non-stock corporation, certain and essential steps must be taken. One cannot be deprived of personal rights without due process of law. And despite by-laws or charter provisions to the contrary, to constitute a legal expulsion, the one expelled must have had notice of the proceeding looking to expulsion; the corporation must have considered the question of expulsion at a meeting regularly had or specially called for that purpose; due formality must have been observed in the proceedings, and finally there must have been a formal conviction resulting from the affirmative action of the required number of members. Discussing these essentials somewhat briefly, the person charged with an offense, the ground of an attempted expulsion, must have notice, not only of the offense with which he is charged, but also of the meeting at which the charge is to be considered by the corporation. He must be given a reasonable opportunity to appear and defend himself against the charges. The meeting at which the charges are considered and the vote of expulsion taken must be held in accordance with charter provisions or the requirements

of a by-law controlling the calling of meetings of the corporation and the business which could be legally transacted at the meeting. The proceedings involving the expulsion must be conducted according to the formalities required by the charter or by-laws. There must be, further, a consideration of the charge and the evidence offered sustaining it in connection with the formal vote of expulsion. The courts hold that there must be proof of the offense charged, even if the defendant fails to appear. In the case of non-stock corporations, where the essentials of a legal expulsion have been carefully observed, the courts, as a rule, will not interfere, unless the rule or by-law authorizing the expulsion was in itself immoral, contrary to public policy or in contravention of the law of the land; or unless the by-law was not observed, or some of the essentials noted above were omitted; and, finally, unless there was bad faith exercised by the corporation and its members in arriving at a decision. The courts will interfere, without doubt where the judgment of expulsion was made without notice and opportunity to be heard. The fundamental principles to be observed in connection with the subject of expulsion of a member from a non-stock corporation are that the personal rights of the individual are protected by constitutional provisions equally with his property rights, and that one cannot be deprived of either without due process of law, and due process of law includes, as its most necessary condition, the giving of notice to one whose rights are to be affected by a proceeding, and affording him, in a court or body of competent jurisdiction, a reasonable opportunity to appear, if he so desires, and protect these rights.

In considering the question of whether an offense prescribed by a by-law as warranting expulsion will, as a matter of law, afford a legal ground for expulsion, many decisions have considered the character of the offense, some holding that only offenses of an infamous character; or, in other words, those which are indictable under the criminal codes of the State, will afford ground for expulsion. Other decisions hold that if a member of the corporation commit

an offense which in and of itself is not indictable or of an infamous character, but which is against the party's duty to the corporation as a member of it, the corporation is warranted in proceeding in a legal manner to expel the member.

§ 90. **Voluntary Withdrawals.** *In Non-Stock Corporations.* In the case of non-stock corporations, the interests of the members in the property of the corporation and their liabilities to corporate creditors, are the principal questions involved. The general rule seems to obtain that by a voluntary withdrawal from a non-stock corporation, the member loses his right to claim any interest in the property of the corporation. He is deemed to have abandoned his property rights. His personal liability of a member in a non-stock corporation for the corporate debts will be considered in a later chapter.

In Stock Corporations. In a stock corporation, upon transfer of ownership and consequent loss of membership, the questions involved are somewhat different. They include the right of the corporation to a lien upon his stock for debts due the corporation, the question of unpaid subscriptions to the capital stock and the right of other shareholders to require him to meet his proportion of the corporate liabilities. These questions will be considered in a subsequent chapter. Upon sale and transfer of the stockholder's interest in the corporation, he is presumed to have received from the purchaser of his interest the equivalent monetary value of that interest in the corporate property.

CHAPTER XI

RIGHTS OF CORPORATE MEMBERS

The powers or rights of corporate members may be somewhat roughly divided into ordinary and extraordinary. Extraordinary rights exercised by members are those which change the original contract of membership and include the power to amend the charter of the corporation; to increase or reduce its capital stock; to sell or lease the entire corporate property, and to consolidate or merge the corporation with others. The courts hold that these powers of the corporation must be exercised, when authorized by law, originally by the stockholders or members of the corporation, and cannot be exercised by the directors without express authority from them.

The ordinary rights or powers appertaining to corporate membership consist of the right to meet and elect directors; to participate in the proceedings at stockholders' meetings; to accept or reject applications for admission, in case of non-stock corporations; to prescribe by-laws; to inspect the corporate books; to participate in the net profits of the corporate business through the payment of dividends; to insist that the corporate property and funds shall not be diverted from their original purpose; to restrain the corporation from doing acts *ultra vires;* to hold officers accountable for their actions in the management of the corporate business; and, in extreme cases, to defend or bring suits or actions at law for and on behalf of the corporation. These powers were indicated in a decision where the judge said:

"The rights of stockholders are: to meet at stockholders' meetings; to participate in the profits of the business; and to require that the corporate property and funds shall not be diverted from their original purpose. If the com-

pany becomes insolvent, it is the right of the stockholders to have the property applied to the payment of its debts. I do not know of any other rights except incidental ones, subsidiary and auxiliary to these. Of course, the stockholder has, ordinarily, the right to a certificate for his stock; to transfer it on the company's books, and to inspect these books. For the invasion of these rights by the officers of the company, he may sue at law or in equity, according to the facts in the case."[1]

A textbook writer has divided the rights of members into individual and collective. The former including a right to a certificate of shares; to transfer his shares; to vote at the stockholders' meeting; to inspect the books of the company; to dividends after the same are declared; and the latter including the right to interfere with corporate management. The more important of these membership rights will be briefly considered in the following sections.

§ 91. Right to a Certificate of Stock. In stock corporations the relation of membership is based upon the ownership of one or more of the aliquot parts into which the capital stock of the corporation is divided. To establish this relation, the possession of a so-called certificate of stock is not necessary, but it is customary for the corporation to issue, as *prima facie* evidence of ownership, a written acknowledgment, under the seal of the corporation and executed by its proper officers, of the ownership of the individual named in the capital stock of the corporation. Every member of a stock corporation is entitled, as a matter of legal right, to this written acknowledgment, and if the corporation refuses to issue it, it has been held that its refusal may be treated as tantamount to a conversion of the shares.

§ 92. Right to Participate in the Management of the Corporation. The right of a member in a stock corporation to share in the general management and conduct of its affairs is limited to participation in stockholders' meetings and to the election of a board of directors or managing

[1] Forbes v. Memphis, etc. R. R., 2 Woods C. C. 323.

officers in whom is vested, usually, the entire power of the direct management of the business affairs of the corporation.

§ 93. Rights in Corporate Property. Incidental to the subject of the right to actively participate in the management of the business of the corporation, the legal doctrine might be stated that the shareholder has no legal title to the property or profits in a corporation until a dividend has been declared or a division made. His interest is merely an inchoate, indivisible, and intangible one. The title to all corporate property is vested in the legal person, viz, the corporation. A stockholder, merely because he may own one-half of the capital stock of a corporation, cannot claim or assert any rights of ownership over one-half of the corporate property. His rights only become tangible and fixed in case of the dissolution of the corporation and a division of its property; or when corporate profits have been formally declared in the form of dividends.

§ 94. Right to Inspect Records. The right existed at common law in every member of a corporation to inspect the books and records of a corporation, at a convenient time and place from the viewpoint of the corporation, and for a proper purpose, either in person or by his properly authorized representative. Many States have passed statutes declaring, as a matter of law, this common-law right. The Minnesota provision is illustrative of acts of this class.[2]

After provision for the keeping of certain accurate and complete records of corporate proceedings, it declares that "All such books and records shall, at all reasonable times and for all proper purposes, be open to the inspection of every stockholder." In Alabama it is provided that "the stockholders of all private corporations shall have the right of access to or inspection and examination of the books of records and papers of the corporation at reasonable and proper times." The wording of the statute in a particular State will determine the exact right of a corporate member,

[2] Rev. Laws of Minnesota, 1905, § 2869.

for, as will be noted in the statement of the common-law rule, this is not an absolute but a limited one.

§ 95. **Right to Inspection.** The fundamental limitations upon the right of inspection on the part of the stockholder are that it shall be exercised at a convenient time and place and for other proper purposes. Even where, by statute, the absolute right is apparently given, certain inherent limitations necessarily exist. These would include an exercise of the right within business hours and at the office of the corporation. The right, further, cannot be exercised in an unreasonable manner, considered from the standpoint of the corporation in the transaction of its business. The right cannot be exercised by the member in such a manner as to prevent the corporation from transacting its business in the usual manner. A corporation with many thousand stockholders—not an unusual condition at the present time—might be entirely prevented from transacting its business if each one of these insisted upon his right to inspect certain corporate books and records, the daily use and keeping of which is absolutely necessary to the carrying on of its business. In the absence of statutes limiting the purpose for which corporate records may be inspected, it has been held that the right is not to be exercised to gratify curiosity or for speculative purposes, but in good faith and for a specific honest purpose and where there is a particular matter in dispute involving and affecting materially the rights of the stockholder. It cannot be exercised at the caprice of the curious and the suspicious. The courts also have held that the right cannot be exercised on account of a general dissatisfaction on the part of the stockholder with the management of the enterprise based upon a vague belief that it is being dishonestly or inefficiently managed. The stockholder has, in general, however, the right to inform himself of all corporate transactions, the right to be exercised under the essential conditions noted above. On this point a New Jersey case[8] held as follows:

"To say that they have the right, but that it can be

[8] Huylar v. Cragin Cattle Company, 40 N. J. Eq. 392

enforced only when they have ascertained in some way without the books that their affairs have been mismanaged, or that their interests are in danger, is practically to deny the right in the majority of cases. Oftentimes frauds are discoverable only by examination of the books by an expert accountant. The books are not the private property of the directors or managers, but are the records of their transactions as trustees for the stockholders."

A further limitation exists upon the right of inspection in this, that even where the stockholders are given by statute the right, yet it does not extend to an inspection of the books or records of the board of directors of the corporation or subcommittees of managing boards. The demand for inspection must be made by the member upon the proper officer in charge of the books or records an examination of which is desired, and the demand must also state, specifically, the particular books or records to be inspected. A general demand for inspection of all the books and records of the corporation is too broad and indefinite.

Remedy for Wrongful Refusal. If, after a proper demand has been made by a stockholder for an inspection of the books and records of a corporation, and upon the proper officer having legal charge or custody of them, the right of inspection is refused, the stockholder has the election of several remedies against the corporation. He can sue it and recover damages sustained, if by competent evidence it appears he has suffered any; he can petition for a writ of *mandamus* to issue against the officer having charge and custody of the books and records in question; or, in those States where a statutory penalty is provided for a denial of the right, this can be recovered.

§ 96. Right to Receive Dividends. It has already been stated that the title to all the corporate property is vested in the corporation and that no stockholder or member has a definite, tangible, or divisible interest before the corporation is dissolved or until a share in the net profits of the corporation has been declared in the form of dividends. The right to receive dividends, if any are earned, belongs

to every stockholder in a corporation organized for pecuniary purposes. A dividend has been defined as a "corporate profit set aside, declared and ordered by the proper corporate officers to be paid to the stockholders on demand or at a certain time." It is the general rule that members have no legal rights to dividends until officially declared, and that they can only be declared and paid out of the net earnings or profits of the corporate business. An implied prohibition, and in many States express, exists against the declaration and the payment of dividends from other sources than the net profits or earnings, for otherwise they may be paid out of the funds representing the capital stock of the corporation. The terms net earnings and profits necessarily have been the subject of many judicial decisions. "The words mean, what shall remain as the clear gain of any business venture after deducting the capital invested in the business, the expenses incurred in its conduct, and the losses sustained in its prosecution."[4] Again, "profits of a company are not such sums as may remain after the payment of every debt, but are the excess of ordinary receipts over expenses properly chargeable to revenue account.[5] Again, "Net earnings are properly the gross receipts, less the expense of operating the road or other business of the corporation. Interest on debts is paid out of what thus remains out of the net earnings; the remainder is the profit of the shareholder."[6]

Discretionary Power of Declaration. The profits of the corporation belong to the corporation. Stockholders have no right to share in them until a certain proportion has been officially declared by the directors as dividends. When the declaration has been made, the common rule seems to obtain that it then cannot be revoked and the corporate member can insist upon its payment if made out of the surplus or the net profits of the corporation. The declaration of dividends rests in the sound discretion of the board of directors or managing officers, and stockholders have no

[4] Park v. Granite, etc., Works, 40 N. J. Eq. 114.

[5] Mills v. Northern, etc., Ry. Co., L. R., 5 Ch. App. 621.

[6] St. John v. Erie R. R., 10 Blatch. 271.

remedy in respect to their action on dividends so long as this discretion is exercised honestly and in furtherance of what the directors, acting upon their best judgment, deem the sound interests of the corporation. Members can complain only when this discretion is abused or the directors act fraudulently. The rule was well stated by the Supreme Court of the United States:[7]

"Money earned by a corporation remains the property of the corporation and does not become the property of the stockholders unless and until it is distributed among them by the corporation. The corporation may treat it and deal with it either as profits of its business or as an addition to its capital. Acting in good faith and for the best interests of all concerned, the corporation may distribute its earnings at once to the stockholders as income; or it may reserve part of the earnings of a prosperous year to make up a possible lack of profit in future years; or it may retain portions of its earnings and allow them to accumulate and then invest them in its own plant, so as to secure and increase the permanent value of its property. Which of these courses is to be pursued is to be determined by the directors with due regard to the conditions of the company's property and affairs as a whole; and, unless in case of fraud or bad faith on their part, their discretion in this respect can not be controlled by the courts, even at the suit of owners of preferred stock, entitled by express agreement with the corporation to dividends at a certain yearly rate in preference to the payment of any dividend on the common stock but dependent on the profits of each particular year as declared by the board of directors."

Form of Dividends and to Whom Paid. It is within the discretion of the board of directors to determine, at the time of the declaration of a dividend, the manner of its payment, whether in cash, stock, bonds or scrip, or property. A dividend can be paid by any of the means suggested, the only limitation being that the funds or property of the corporation representing its capital stock cannot be distributed in the form of dividends. In stock corporations

[7] Gibbons v. Mahon, 136 U. S. 549.

the universal rule prevails that the member whose name appears on the books of the company at the time designated in the declaration of the dividends, is entitled to receive it. The stock transfer books, except in special cases, determine absolutely the rights of parties in this respect, and the corporation is fully protected in paying dividends to the members then appearing upon its records.

§ 97. Right to Vote. This is also one of the ordinary rights of the member of a corporation. In a non-stock corporation each member is entitled to one vote, and this was the common law also in respect to the right of members in stock corporations. The rule, however, has obtained for many years that members of stock corporations are entitled in person or by proxy to that proportion of votes in stockholders' meetings represented by the number of shares appearing in their names upon the books of the company. In cases of dispute, only shareholders of record are entitled to vote, and the transfer books of the corporation are universally regarded as *prima facie* evidence of the right. In cases of transfer the vendor may exercise his right of voting until the vendee has completed the transaction by causing to be transferred upon the books of the company his name as the owner of the stock.

Cumulative Voting. As stated above, the common rule prevails at the present time that the shareholder is entitled to that number of votes corresponding with the number of shares appearing in his name upon the books of the corporation. The usual manner of casting these votes has been modified of recent years by custom, and also by statute in many cases, through the introduction of what is known as the cumulative system of voting. Unless this prevails, the power of the majority is absolute. They can elect the entire board of directors or managing officers. The minority interests, although representing, for illustration, 49 per cent of the capital stock, will be deprived of representation upon the board. To enable a minority interest to obtain representation, the system above has been introduced, and this, in effect, gives to the minority

shareholders the power to elect members of the board of directors by accumulating their votes on one or more candidates. To illustrate: Suppose there are five directors to be elected; the majority of shareholders have seven hundred votes, the minority three hundred. It is apparent that the majority can cast seven hundred for each of their five candidates. The minority, under the cumulative system, may multiply their entire number of votes by the number of directors to be chosen (three hundred times five) and cast the entire fifteen hundred votes for two candidates, thus assuring their election over two of the candidates of the majority.

§ 98. Rights of Stockholders over Corporate Action. Other rights of stockholders are to hold corporate officers accountable for their actions in the management of corporate property, and, in extreme cases, to defend and bring suits for the corporation. A quotation from a leading case decided by the Supreme Court of the United States, dealing with the exercise of these rights, will sufficiently and clearly state the law on the question involved:[8]

"Before an action can be maintained by the stockholder there must be shown: (1) Some action or threatened action of the directors or trustees which is beyond the authority conferred by the charter, or the law under which the company was organized; (2) such a fraudulent transaction, completed or threatened by them, either among themselves or with some other party, or with shareholders, as will result in serious injury to the company or the other shareholders; (3) that the directors, or a majority of them, are acting for their own interest in a manner destructive of the company, or the rights of the other shareholders; (4) that the majority of the shareholders are oppressively and illegally pursuing, in the name of the company, a course in violation of the rights of the other shareholders which can only be restrained by a court of equity; (5) it must also be made to appear that the complainant made an earnest effort to obtain redress at the hands of the directors and shareholders of the corporation, and that the ownership was vested in him at the time of the transactions of which

[8] Hawes v. Oakland, 104 U. S. 450.

he complains, or was thereafter transferred to him by operation of law."

In restraining *ultra vires* acts, the court, in a New York case, said:[9]

"We do not question the right of stockholders to complain of any diversion of the capital and assets to purposes not authorized by the charter, and to arrest by suit an unauthorized course of dealing which results in such diversion. The powers of a court of equity may be put in motion at the instance of a single shareholder, if he can show that the corporation is employing its statutory powers for the accomplishment of purposes not within the scope of its institution."

And, on the points directly involved in this section the court, in the same case, said:

"In action by stockholders, which assail the acts of their directors or trustees, courts will not interfere unless the powers have been illegally or unconscientiously executed, or unless it be made to appear that the acts were fraudulent or collusive and destructive of the rights of the stockholders. Mere errors of judgment are not sufficient as grounds for equity interference; for the powers of those entrusted with corporate management are largely discretionary."

[9] Leslie v. Lorillard, 110 N. Y. 519.

CHAPTER XII

MEMBERSHIP LIABILITY

§ 99. **Liability of Members of Stock Corporations.** Membership liability may be broadly divided into liability to the corporation, liability to other members, and liability to corporate creditors. This liability is entirely contractual, and so depends upon the terms of the agreement between the members and the corporation. Liability to the corporation will be first considered.

To the Corporation. The articles of incorporation fix the amount of its capital stock, the number of shares into which it is divided, and their par value. One of the contract obligations entered into at the time of the organization of the corporation is the agreement between the members and the corporation that they will pay into the corporate treasury, for the purpose of carrying on its business and for the payment of corporate debts, in money or in money's worth the full par value of the stock subscribed by them.

The liability, therefore, exists on the part of the original stockholders of the corporation to pay on call amounts remaining unpaid on their stock up to the par value thereof. This liability attaches only to the original holders of the corporate stock and their vendees with knowledge that a balance remains unpaid upon the stock. A *bona fide* purchaser on the open market, having no knowledge of the fact that a portion of the par value of the stock remains unpaid, is not subject to the liability. The corporation itself can, by contract with its members, relieve them from the payment of a part of the par value of the stock, though such an arrangement will not ordinarily

be binding upon the creditors of the corporation. As to the latter, the obligation to pay par for stock remains.

A shareholder may become indebted to the corporation personally by a transaction between them, but this is not regarded as a membership liability in the ordinary sense.

When the obligation called for by the subscription to the shares of stock of a corporation is performed, it has no farther rights which it can enforce against the member. The contract of subscription determines and measures the liability of a shareholder to the corporation.

To Other Shareholders. One of the distinctive characteristics of a private corporation is, that between the members there does not exist a trust relation when the contrary rule obtains in other forms of association by natural persons. The liability to pay par for the stock runs from the individual member to the corporation itself, and not to the other members. If any one of them fail to perform this contract, a personal liability to the other members will not be created. The courts have, however, held, that the members of a corporation are engaged in a common enterprise. One of the rights of a stockholder, it will be remembered, was that of receiving dividends, and the existence of this right carries with it a corresponding liability to share in the financing of the corporation. Members failing to pay the full par value of their stock into the corporate treasury may be compelled by the other stockholders, because of the community of interest and of obligation noted above, to respond to their contract obligations.

The courts have also held that members of a corporation can have set aside secret arrangements by the corporation with other members by which they are to receive their stock on more favorable terms.

To Creditors. The liability of stockholders in a corporation to the corporate creditors is commonly divided into statutory or constitutional, and other than statutory or constitutional. The latter includes common-law liability, so-called, and what is known as a partnership liability.

Partnership Liability When Corporate Organization is

Defective. In a preceding chapter the importance was suggested of the ability to determine when a legal corporation existed, this, from the standpoint of a natural person, forming one of a group of persons associated in a corporate capacity. The liability of a stockholder in a corporation for the corporate debts being a limited or restricted one when compared with that of a natural person or a co-partnership. The corporate relation established, the extent of the liability is consequently established. When the required tests of a legal incorporation are applied and affirmatively answered, a legal corporation exists whose corporate rights in this respect cannot be questioned even by the State. In the creation of corporations, informalities and irregularities may occur which, while they deprive it of the character of a corporation *de jure,* do not take away its right to exist as a corporation and act in a corporate capacity, a corporation of the latter class being known as one *de facto.* The attempt on the part of a group of natural persons to organize a corporation may, however, not be made in good faith; or the irregularities and informalities may be so grave that even a *de facto* corporation is not created. The liabilities of the members of a defective corporation of this kind will be those of a co-partnership. In some cases, also, the courts have held, that the liabilities of those organizing a corporation for obligations incurred prior to incorporation will attach to them as co-partners, unless expressly adopted or assumed by the corporation upon its organization. It might be said that the law is steadily tending to the establishment of at least a *de facto* corporation, unless the informalities and irregularities are so grave in character as to prevent this holding, or unless some of the other essentials of a *de facto* corporation do not exist.

§ 100. Common-Law Liability. The entire obligation of the member of a corporation to it and its creditors is measured by his contract of subscription to the shares of stock of the corporation. This contract of subscription called for the payment in money or in money's worth to

the corporation by the stockholder of the par value of the stock. Upon failure to perform the obligation of this contract as to payment, the corporation could enforce its terms against the stockholder. The contract obligation to pay par for the stock by the original subscriber is known as the common-law liability. It exists, not as a matter of statutory or constitutional provision, but by reason of the terms of the contract made by the subscriber. In some States, constitutional and statutory provisions have been adopted or passed holding a stockholder liable for the debts of the corporation to the extent of the par value of the stock. These provisions are merely declaratory of the common law. The obligation to pay par for the stock exists independent of statutory or constitutional provisions. By arrangement between the corporation and the stockholder, the latter may be relieved of a part of this obligation. A release, however, of this character, will not affect the rights of the corporate creditors who can enforce in some proceeding the payment by the stockholder of the full par value of his stock.

§ 101. **Liability for Capital Wrongfully Distributed.** It has been a common holding of the courts that the capital stock of a corporation is a trust fund, to be maintained by it at parity for the benefit of the corporate creditors. The trust fund theory will be fully discussed later, but attention is called to it here for the reason that it may involve the liability of a stockholder to creditors in case they have permitted the property of the corporation, or an equivalent value of its capital stock, to be distributed among themselves to the injury of the corporate creditors. The courts hold without exception that where this has been done the corporate stockholders will be liable in proportion to their stock holdings to the extent of the property wrongfully and illegally distributed. This liability, it will be noted, is the application of the common-law liability, so-called, to circumstances or conditions not originally arising. The common-law obligation is that the stockholder shall pay to the corporation the par value of his stock for the benefit

of the corporate creditors. If, after having paid this, he permits the fund thus created to become illegally diminished, it will be regarded, on his part, as if he had not complied with his common-law obligation. "The stockholders have no right to anything but the residuum of the capital stock after the payment of all the debts of the corporation. If, before all such debts are discharged, they take into their hands any of the funds of the corporation, they hold them subject to an equity which is against conscience to resist."[1]

§ 102. **Statutory or Constitutional Liability.** In nearly all of the States, by constitutional or statutory provision, there has been established a stockholders' liability in excess of or beyond that created and existing by reason of the contract of subscription; viz, the common-law liability. In some States these provisions exist providing for a liability to the full par value of the stock, but these have been commonly construed as simply declaratory of the common law. The phraseology of constitutional and statutory provisions relative to stockholders' liability varies, and the particular meaning of words used and the application of them must be learned by consulting the decisions of a particular State. They impose, usually, a liability in addition to the common law liability. They are not to be extended by implication, and the courts usually apply strict rules of construction in their application, since they are in derogation of common law. The Constitution of Minnesota, Article 10, Sec. 3, provides: That "each stockholder in any corporation, excepting those organized for the purpose of carrying on any kind of manufacturing or mechanical business, shall be liable to the amount of stock held or owned by him." This provision establishes what is commonly known as a double liability and is illustrative of a large number of similar enactments. There is, necessarily, a great diversity, as above stated, in the character of the liability created by statutory or constitutional pro-

[1] Kohl v. Lillienthal, 81 Cal. 378.

vision in excess of or beyond the common-law liability. A recent textbook states concisely their effect:[2]

"The liabilities thus imposed, may, however, be roughly classified as follows: (1) A joint and several liability as partners; (2) a joint and several liability as guarantors; (3) a limited and several liability to be enforced absolutely or, more commonly, upon regular proceedings against the corporation proving ineffectual. The first class abrogates entirely the rule of limited liability and is governed by the law of partnership. The member becomes a principal debtor. Under the second class the liability is secondary and collateral to that of the corporation, and is governed in a general way by the rules of guaranty. Thus, any act on the part of the creditors that will release a guarantor will release a stockholder from his liability. The liability under the third class is ordinarily limited to (a) an amount equal to the shares of capital stock held by the member; or (b) an amount equal to the ratio which the member's proportion of the capital stock bears to the entire corporation indebtedness. 'The distinctive characteristic of this liability is that each member stands liable for a definite sum and no more, irrespective of the amount for which the others are liable. It is a several, unequal, and limited liability as to which each member stands alone, except that, if he pays more than his proportion of the debts of the company, he may, as in other cases, have contribution from his fellow shareholders.'"

Constitutional Provisions: When Self-Executing. Constitutional provisions imposing an additional liability are self-executing, as the phrase is used, when they require no additional action by the legislature to make them available to creditors. A constitutional provision not self-executing, must be supplemented by legislation to become operative. Its character in this respect will be ascertained from its language and the intent as gathered from the circumstances and the conditions attaching to its adoption; if the phraseology of the provision is general or the extent of the liability not fixed, legislation will be necessary. The decisions in the different States are at variance in the construction of constitutional provisions similarly worded. In discussing

[2] Abbott's Elliott on Private Corporations, 4th ed. § 558.

the question of whether a constitutional provision was self-executing, Justice Mitchell, in a case which is frequently cited, said:

"A constitution is but a higher form of statutory law, and it is entirely competent for the people, if they so desire, to incorporate into it self-executing enactments. These are much more common than formerly, the object being to put it beyond the power of the legislature to render them nugatory by refusing to enact legislation to carry them into effect. Prohibitory provisions in a constitution are usually self-executing to the extent that anything done in violation of them is void; but instances of affirmative self-executing provisions are numerous in almost every modern constitution."[3]

Exemptions. While the State encourages the organization of all private corporations, it may especially favor those formed for manufacturing and other purposes, the transaction of the business of which tends more immediately and directly to the building up and to the advantage of a community. In some States this attitude has been exhibited by excepting from the operation of constitutional or statutory provisions imposing an additional liability the stockholders of these corporations. The constitutional provision of Minnesota is illustrative of the statement. An exception there is made of corporations organized for mechanical and manufacturing purposes. In respect to these, there exists but the common-law liability; as to all others, a double liability.

Power to Create Membership Liability. It is clearly within the power of the State, in a valid exercise of its power of regulation, to adopt or pass the constitutional or statutory provisions noted in a preceding section, establishing an additional liability on the part of the corporate members for the debts of the corporation. The only possible limitation may arise when the State, in the grant of a charter, has specifically limited membership liability. A grant of this character will be construed as a part of the contract between the State and the corporation and its members,

[3] Willis v. Mabon, 48 Minn. 140.

the obligation of which cannot be impaired by any subsequent act of the State. If the power to alter, amend, or repeal has been reserved, this limitation is eliminated.

Nature of Liability. A statutory or constitutional liability may either be contractual or penal in its nature. This fact is important as affecting the rights of the creditors to pursue available remedies in the enforcement of their claims against the corporation. The language and purpose of the enactment determines, ordinarily, its nature as contractual or penal, and the decisions of the courts in the different States must be examined to determine the question when it arises. The Minnesota provision already quoted is contractual in its nature. And, on the other hand, a liability imposed upon stockholders, officers, or agents of a corporation for a failure to comply with the provisions of law in respect to the filing and publishing of certain designated reports has been held to be penal. The liability imposed upon stockholders in national banks is contractual in its nature, and it has also been held that this survives against the personal representatives of the stockholder. Whether a provision creating an additional stockholders' liability is contractual or penal affects also the right of the creditor to enforce the liability against stockholders residing in other States than that under the laws of which the corporation has been created, the common rule being that penal statutes have no extra-territorial force. A penal liability is incapable of enforcement against a stockholder in a foreign state.

Meaning of Word "Debts" and Similar Phrases. In statutory and constitutional provisions, the words "debt," "debts," "obligations," and other words or phrases of similar import are used in respect to which the additional liability can be enforced against stockholders. Naturally, the proper and legal significance of these words or phrases has been the occasion of judicial construction by the courts. The words are commonly applied to the debts of the corporation contracted or existing at a designated time, and are usually held to apply to obligations *ex-contractu*

and not to obligations which result from a tort of the corporation.

There are, however, several jurisdictions which hold to the contrary and construe the words as applying both to obligations contractual in their nature and also claims for damages sounding in tort. In some instances the liability applies only to debts due laborers and employes. The common construction here is that the additional liability is confined to claims based upon manual or menial service. The additional stockholders' liability cannot be enforced, for illustration, to satisfy a claim for unpaid salary by an assistant superintendent or attorney.

To Whom Liability Attaches. The usual rule prevails that the additional or stockholders' liability established by a constitutional or statutory provision attaches to the registered stockholder; that is, the one whose name appears upon the stock books and records of the company as sustaining to the corporation the relation of membership. This rule has been modified in some cases where a transfer has been made by a solvent member for the purpose of avoiding his stockholders' liability. A transfer for this purpose is termed a colorable transfer, and has been defined as one which is technically and legally correct, but made for the purpose of defrauding creditors. If a transfer is made to what is known as a straw man, or to a person *non sui juris,* or to the corporation, although the transfer be technically made, the creditors can hold, if they elect, the transferrer of the stock. A colorable transfer may also exist where stock has been transferred as a gift to others when the transaction results in a fraud upon creditors, although, if the gift is made in good faith by the former stockholder, the transfer will be sustained.

In some States, also, by statute, the creditor is given a designated time within which he can elect to hold either the transferor or the transferee, even where the transfer is made in good faith and for a valuable consideration, and not for the purpose of avoiding stockholders' liability or defrauding the creditors of the corporation. An illustra-

tion of an act of this character is to be found in the Rev. Laws of Minnesota, 1905, Sec. 2985, where it is provided that "every person becoming a stockholder (in a bank) shall succeed, in proportion to his interest, to all the rights and become subject to all the liabilities of his transferor, but the liability of the latter shall continue for one year after the entry of such transfer."

Statutory provisions also exist in many States which, in effect, provide that a transfer of stock shall not in any way exempt the person making such transfer from any liabilities of the corporation which were created prior to the transfer. In respect to colorable transfers, it might be said, however, that the law is steadily tending to the protection of the *bona fide* owner who purchases on the open market and for a valuable consideration.

Stock Held in Fiduciary Capacity. Where stock appears upon the books of the company in the name of a person as trustee, liability attaches to the estate, and where one holds stock as an executor or administrator the estate is held liable, in many States, by express statutory provision. Where stock is held by one in a trust capacity, or as agent for another, in the absence of facts or record entries stating the relation, the rule is that the creditor can elect to hold either the one whose name appears as the registered stockholder, the *cestui qui trust,* or the undisclosed principal. A stockholder may be also estopped to deny his relation where he exercises rights and accepts the benefits of membership in the corporation, although no formal transfer has been made upon the books of the company; and the courts have also held, in protection of a transferor, who has in good faith made a transfer of his stock, that where the transferee or the corporation have negligently failed to make proper and complete entries on the books of the corporation, that the transferee will be held to the stockholders' liability.

Enforcement of Liability. The extent and the nature of stockholders' liability established by constitutional or statutory provisions is created and attaches, undisputably,

as the result of them. They vary so widely in the different jurisdictions that it is impossible to state any general rule or principle which will be of material assistance to the reader upon the subject of this section. In some States the creditor is authorized to proceed directly against the stockholder for the enforcement of the liability. In others, the common remedy is of an equitable nature where all the stockholders and creditors are brought into court and the debts equitably adjusted. The liability is generally a secondary one, although in some States it is made a primary obligation on the part of the stockholder. Where it is secondary, the universal rule obtains that a liability can only be enforced against a stockholder after a judgment has been obtained against the corporation and an execution returned thereon *nulla bona* (no property). The creditor must first exhaust all means for the collection of his debt against the corporation before he can proceed to enforce the stockholders' liability. A judgment obtained by him against the corporation is usually held to be conclusive upon the question of corporate indebtedness in subsequent proceedings against the stockholders to enforce his liability. No general rule can be stated by which can be accurately determined the proper person to enforce the liability. This will depend, again, on statutory provisions. The decisions of a particular court and the statutes relating to stockholders' liability must be examined and followed. It is not common, however, to regard a stockholder's liability as an asset of the corporation in the common acceptation of that term. In some States, a receiver of the insolvent corporation is the proper party to enforce the statutory liability of stockholders.

In Foreign Jurisdictions. The decisions in respect to the right to enforce a stockholder's liability in foreign jurisdictions are unsatisfactory and conflicting. If the liability is contractual in its nature, many foreign jurisdictions permit its enforcement against non-resident stockholders. The right is construed and determined according to the *lex loci contractus* and the remedy must be followed and

construed according to the law of *lex loci* (law of the place) *forum*. The right in a foreign state to enforce a stockholder's liability has been construed liberally in some States and strictly in others; so narrow in some cases as to practically deprive creditors of a part of the security on which their debts were contracted. It is universally admitted that where the liability is penal in its nature, it cannot be enforced outside the State creating the liability. The decisions, in establishing the character of the law creating a stockholder's liability as contractual or penal, hold that it is the effect and not the form of law which determines this. A penal law has been defined as one which directs or prohibits some act and imposes some forfeiture for its transgression.

§ 103. Shareholder's Liability. When proceedings are brought to enforce a stockholder's liability, while the common rule obtains that the registered stockholder is the one ordinarily liable, yet the time when the debt was contracted may change the rule, and the decisions involving a determination of this point are numerous and conflicting, the result of contrary statutory provisions in many cases even in the same State. The statutes and decisions in each jurisdiction, at the time it is necessary to determine the question, must be examined to ascertain the correct rule of law to be applied at a specific time. In general, it might be said, that there are three lines of decisions, in main the result of the varying conditions noted above, one line holding that the stockholders who were such at the time the debt was contracted will be liable, and a transfer will only release them from debts subsequently incurred. A transfer will not release them from those incurred by the corporation during their membership. Another line of decisions is to the effect that a registered stockholder at the time when the proceedings were commenced to enforce liability, is alone liable. And still other decisions hold that all persons are liable as stockholders who sustained that relation to the corporation either at the time the debt was contracted, or who became such prior to commencement of the action.

§ 104. Stockholders' Defenses. The defenses or rights available to stockholders in cases of proceedings brought to enforce their statutory liability are usually the statute limitations, if applicable, a claim against the corporation, or set-off as it is termed, and the right of contribution from other members of the corporation. In the absence of statutory provisions granting the right, a stockholder is not permitted to set off against his statutory liability a claim in his favor against the corporation. The character of the liability as primary or secondary will govern the application of the statute of limitations. If primary, the obligation rests upon the stockholder at the time the debt is contracted and the statute of limitations commences to run at the time the debt is due. If secondary, the statute begins to run from the time the insolvency of the corporation is determined. If the liability is penal in its character, it will be governed by the statute of limitations in a particular State relating to penalties and forfeitures. Where a statutory liability is joint and several, if contractual, a stockholder who has been obliged to pay more than his proper proportion to liquidate the debts of the corporation is entitled to contribution from the other stockholders, but otherwise if the liability is penal.

CHAPTER XIII

CAPITAL STOCK

§ 105. **Definition and Nature.** The capital stock of a corporation is the amount fixed by the corporate charter as the sum paid in or to be paid in by the stockholders for the prosecution of the business of the corporation and for the benefit of corporate creditors. The capital stock of a corporation is to be clearly distinguished from its capital. Capital is wealth in use. It is that part of a man's stock which he expects to afford him a revenue, as defined by Adam Smith. The capital of a corporation consists of the sums paid in by the stockholders, increased by profits of the corporate business, and diminished by its losses. The capital stock of a corporation does not vary but remains fixed, although its capital may fluctuate widely in value, diminished by losses or increased by gains.

§ 106. **Shares of Stock: Stockholder.** The term stockholder indicates one who owns stock in a corporation and has been accepted as a member by it. He is one who owns one or more of the aliquot parts of the shares of stock into which the capital stock of the corporation is divided. He is an individual distinct and separate from the corporation in all its contracts and the transaction of its business. The corporation is the legal entity; its business is transacted in the name of the corporation and the title to its property is vested in the corporation. All rights resulting from the existence of a corporate capacity and the transaction of corporate business exclusively belong to it and are vested in the corporation as a legal person. A certificate of stock is the written acknowledgement by the corporation, under its seal, of the ownership by the person designated of one or more of the aliquot parts into which its capital stock is divided. Its possession is not necessary to constitute a

person a stockholder. It is the legal fact of ownership which establishes the relation.

Nature of Shares of Stock. Shares of stock are universally regarded as personal property, and this is true although all the property of the corporation may consist of real estate. A share of capital stock, though personal property, is not a chattel. It is, as some authorities declare, property in the nature of a chose in action. Its character is such that it ordinarily cannot, either by act of law or of its owner, be taken into tangible possession by its owner. It is representative merely. The certificate of stock, as evidence of that ownership, may, however, be taken into tangible possession. The certificate of stock is *prima facie* evidence of the ownership of the particular property designated. It transfers nothing from the corporation to the stockholder, but merely affords the latter evidence of his rights. A certificate of stock, further, it should be clearly understood, is not the stock, but merely evidence of the ownership of shares. Certificates of stock are not, in the true meaning of the words, negotiable instruments, though they are commonly regarded as quasi-negotiable.

The Statute of Frauds controls sales of capital stock since it is regarded as personal property, and its provisions must be complied with. On the death of the stockholder shares are distributed as personal property and divided according to statutory provisions relative to the distribution of property of that character. Statutory provisions declaring the nature of shares of stock as personal property are common in all the States.

§ 107. Classification of Capital Stock. In the absence of statutory prohibitions, a corporation upon its organization may divide its capital stock into as many classes as the organizers may elect, which are known by names usually indicating their peculiar rights and characteristics. The usual classification, if different kinds are provided for, is that into common and preferred. By common stock is meant that which entitles the owners to an equal *pro rata* division of the profits, if any there be, one stockholder, or

class of stockholders, having no advantage, priority or preference over other stockholders in the division. By preferred stock is understood that which entitles its owners to some special right or priority over the holders of the common stock. The priority, preference, or advantage may consist in the right to receive dividends from the corporate profits before the holders of the common stock are entitled to any. The dividend rate may be a maximum one fixed by the articles of incorporation, or the rate to be paid may be left to the discretion of the board of directors or managing officers. It may be either cumulative or non-cumulative. If of the former class, all arrears of dividends on the preferred stock must be paid from the profits of subsequent years before the holders of common stock are entitled to receive dividends. If non-cumulative, the dividends paid to holders of preferred and common stock are determined and paid from the profits of corporate business of each fiscal year. The priority, preference, or advantage again may consist in other rights granted to the holders of the preferred stock. They may be entitled, for illustration, to elect a majority or a prescribed number of the board of directors, irrespective of the proportion which it bears to the total capital stock. Or the advantage may consist in rights granted to the holders of preferred stock to receive, upon a dissolution of the company, from the sales of the corporate property, after the payment of corporate debts, a reimbursement of the sums paid by them for their stock before anything can be paid to the holders of the common stock. To summarize, the rights usually granted to holders of preferred stock consist of a priority or a preference in respect to dividends, voting, or a division of corporate property upon dissolution. The preferences in respect to dividends and division of property are those commonly given.

Status of Preferred Stockholder. It must be understood, however, that because the holders of preferred stock are entitled to priority in the payment of dividends that they are legally entitled to them if the corporation has

not earned profits which can be properly applied to their payment. Dividends, both on preferred and common, or other classes of stock, must be earned, otherwise the corporate creditors have the legal right to enjoin the payment of dividends where, by so doing, they can prove that a portion of the sum representing the capital stock of the corporation will be illegally distributed and their security, therefore, impaired or diminished. If the dividends upon the preferred stock are cumulative, a holder of that stock has the right to prevent payments to common stock before the arrears are made up. A preferred stockholder, where his priority consists of a preference in respect to the payment of dividends, is not considered a creditor of the property or the assets of the corporation upon its insolvency, and he is not entitled to any arrears of dividends upon his preferred stock in case of insolvency as a creditor of the corporation. On the question of the right to cumulative dividends, a New York court[1] said:

"The reasonable and fair interpretation of the contract (referring to the priority in dividends on preferred stock) is that the dividends were not only to be preferred, but being guaranteed, were cumulative and a specific charge upon the accruing profits, to be paid as arrears, before any other dividends were divided upon the common stock. The doctrine that preference shares are entitled to be first paid the amount of dividends guaranteed and of all arrears of dividends and interest before the other shareholders are entitled to receive anything, and although they can receive no profits where none are earned, yet, as soon as there are any profits to divide, they are entitled to the same, is fully supported by authority."

§ 108. Declaration of Dividends within Discretion of Managing Officers. As already stated, no dividends can be paid to any class of stockholders except from the net earnings or profits of the corporation, and the declaration of dividends is left, in all cases, to the discretion of the board of directors or managing officers. They may apply

[1] Boardman v. Lake Shore, etc., Ry. Co., 84 N. Y. 157.

the net profits or earnings of corporate business toward the payment of debts, the enlargement of the corporate plant, the accumulation of a cash surplus or reserve, if, in the exercise of their best and honest business judgment and discretion such a course is advisable, rather than in its distribution in the form of dividends to the stockholders of the corporation.

§ 109. Trust Fund Theory. In an early case,[2] Justice Story declared that the capital stock of a corporation is a trust fund in the hands of the corporation for the payment of its debts, and that the corporation stands in the relation of a trustee to the creditors and the shareholders of the corporation. This doctrine was attempted to be applied in many subsequent decisions in its technical meaning, but it is quite evident that Justice Story did not so intend, but used the language in its general sense and under the limitations which have since been stated by the Supreme Court of the United States and in many other jurisdictions. The true basis upon which the property of a corporation is held, both for its creditors and for its stockholders, is well stated in a recent case in the Supreme Court of the United States,[3] where the court, after referring to various decisions in which the phrase trust fund was used, and the trust fund doctrine applied, said:

"While it is true language has been frequently used to the effect that the assets of a corporation are a trust fund held by a corporation for the benefit of creditors, this has not been to convey the idea that there is a direct and express trust attached to the property. . . . A corporation is a distinct entity. Its affairs are necessarily managed by officers and agents, it is true; but, in law, it is as distinct a being as an individual is, and is entitled to hold property (if not contrary to its charter) as absolutely as an individual can hold it. Its estate is the same, its interest is the same, its possession is the same. Its stockholders may call the officers to account, and may prevent any malversation of funds, or fraudulent disposal of property on their

[2] Wood v. Dummer, 3 Mason, C. C. 308.

[3] Hollins v. Brierfield Coal & Iron Co., 150 U. S. 371.

part. But that is done in the exercise of their corporate rights, not adverse to the corporate interests, but coincident with them.

"When a corporation becomes insolvent, it is so far civilly dead, that its property may be administered as a trust fund for the benefit of its stockholders and creditors. A court of equity, at the instance of the proper parties, will then make those funds trust funds, which, in other circumstances, are as much the absolute property of the corporation as any man's property is his."

In a Minnesota case,[4] in an opinion by Justice Mitchell, the court said:

"This trust fund doctrine, commonly called the American doctrine, has given rise to much confusion of ideas as to its real meaning, and much conflict of decision in its applications. To such an extent has this been the case that many have questioned the accuracy of the phrase, as well as doubted the necessity or expediency of inventing any such doctrine. While a convenient phrase to express a certain general idea, it is not sufficiently precise or accurate to constitute a safe foundation upon which to build a system of legal rules. . . . The phrase that 'the capital of a corporation constitutes a trust fund for the benefit of creditors' is misleading. Corporate property is not held in trust, in any proper sense of the term. A trust implies two estates or interests, one equitable and one legal; one person, as trustee, holding the legal title, while another, as the *cestui que trust,* has the beneficial interest. Absolute control and power of disposition are inconsistent with the idea of a trust. The capital of a corporation is its property. It has the whole beneficial interest in it, as well as the legal title. It may use the income and profits of it, and sell and dispose of it, the same as a natural person. It is a trustee for its creditors in the same sense and to the same extent as a natural person, but no further."

"The trust fund doctrine only means that the property of the corporation must first be appropriated to the payment of the debts of the company before any portion can be distributed to the stockholders; it does not mean that the property is so affected by the indebtedness of the company, that it can not be sold, transferred, or mortgaged to *bona*

[4] Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174.

fide purchasers for a valuable consideration, except subject to the liability of being appropriated to pay that indebtedness. Such a doctrine has no existence."[5]

§ 110. **Watered or Bonus Stock.** By watered or bonus stock is meant that which is issued as fully paid up, when in fact the whole amount of the par value thereof has not been paid in. It is, accordingly, stock which purports to represent but does not represent, in good faith, money paid into the treasury of the company or money's worth, or services rendered and actually contributed to the working capital of the corporation. It will be remembered that the contract of subscription between the original stockholder and the corporation upon its organization was to pay into the corporate treasury, for its benefit and the benefit of the corporate creditors, money or money's worth to the full par value of the stock. This contract obligation is used as the basis of the common law liability on the part of stockholders.

To prevent a fictitious increase in the stock or indebtedness of the corporation, many States have, by constitutional or statutory provisions, prohibited the issuing of capital stock or evidences of indebtedness except for money, property, or services or money's worth received by the corporation. The constitutional provision of Illinois,[6] is illustrative of this class of prohibitions, "No corporation shall issue stock or bonds except for money, labor done, or money or property actually received, and all fictitious increase of stock or indebtedness shall be void." In the absence of statutory or constitutional provisions, as a rule the issue of stock of this character is not held unlawful. The legal argument against the issue of watered or bonus stock is based upon the proposition that the transaction is a fraud upon the creditors.

Liability of Stockholder on Watered or Bonus Stock. The capital stock of a corporation unimpaired is supposed to be represented by its full par value in corporate property

[5] Abbott's Elliott on Private Corporations, § 318.

[6] Illinois Const., Art. 11, § 13.

and constitutes a fund for the payment of its corporate debts. The issue of capital stock as fully paid up, when this is not the fact, may, under certain conditions, mislead and perpetrate a fraud upon those dealing with the corporation. Even in the absence of a statutory or constitutional prohibition, the decisions establish the doctrine that it is not every creditor who can complain because of the issue of watered or bonus stock. The test of his right to complain is whether he was injured by the act of the corporation. It is well settled that an equity in favor of a creditor does not arise absolutely and in every case to have the holder of watered or bonus stock pay for it contrary to his actual contract with the corporation. No such equity exists in favor of one whose debt was contracted prior to the issue, since he could not have trusted the company upon the faith of such stock.[7] Again, an equity in favor of a subsequent creditor cannot exist where he has dealt with the corporation with a full knowledge of the conditions and circumstances under which it was issued, and the fact of the issue of watered or bonus stock, for no one can be defrauded by that which he knows of when he acts. If the corporation having watered or bonus stock incurs a debt, a creditor with full knowledge clearly cannot complain.[8]

The doctrine that no equity exists in favor of a corporate creditor to have the holder of bonus or watered stock pay its full par value to the corporation has also been applied in cases where stock has been issued and sold at its full market value, though less than par, to pay the corporate debts; or where an active corporation, whose original capital has been impaired, for the purpose of recuperating itself, issues new stock and sells it on the market for the best price obtainable though less than par.

In each of the instances above noted, the trust fund theory has been applied by some courts, but the weight of

[7] Coit v. Gold Amalgamating Company, 119 U. S. 343; Handley v. Stutz, 139 U. S. 417.

[8] First National Bank v. Gustin, Minerva, etc., Mining Co., 42 Minn. 327.

modern authority follows the application of that rule as stated in Hollins v. Brierfield Coal & Iron Co. cited above. In the Minnesota case above cited, Hospes v. Mfg. Car Co., Justice Mitchell, in explaining the trust fund doctrine as applied to bonus or watered stock, said:

"It is difficult, if not impossible, to explain or reconcile these cases upon the trust fund doctrine, or, in the light of them, to predicate the liability of the stockholder upon that doctrine. But by putting it upon the ground of fraud, and applying the old and familiar rules of law on that subject to the peculiar nature of a corporation and the relation which its stockholders bear to it and to the public, we have at once rational and logical ground on which to stand. The capital of a corporation is the basis of its credit. It is a substitute for the individual liability of those who own its stock. People deal with it and give it credit on the faith of it. They have a right to assume that it has paid-in capital to the amount which it represents itself as having; and if they give it credit on the faith of that representation, and if the representation is false, it is a fraud upon them; and, in case the corporation becomes insolvent, the law, upon the plainest principles of common justice, says to the delinquent stockholder, 'Make that representation good by paying for your stock.' It certainly cannot require the invention of any new doctrine in order to enforce so familiar a rule of equity. It is the misrepresentation of fact in stating the amount of capital to be greater than it really is, that is the true basis of the liability of the stockholder in such cases; and it follows that it is only those creditors who have relied, or who can fairly be presumed to have relied, upon the professed amount of capital, in whose favor the law will recognize and enforce an equity against the holders of bonus stock."

The leading case on the right of a corporation, whose capital stock has been impaired, to issue stock and place it upon the market at less than its par value, is Handley v. Stutz, cited above, where the court said:

"The case then resolves itself into the question whether an active corporation, or, as it is called in some cases, a 'going concern,' finding its original capital impaired by loss

or misfortune, may not, for the purpose of recuperating itself and providing new conditions for the successful prosecution of its business, issue new stock, put it upon the market, and sell it for the best price that can be obtained. . . . To say that a corporation may not, under the circumstances above indicated, put its stock upon the market and sell it to the highest bidder, is practically to declare that a corporation can never increase its capital stock by a sale of shares, if the original stock has fallen below par. The wholesome doctrine, so many times enforced by this court, that the capital stock of an insolvent corporation is a trust fund for the payment of its debts, rests upon the idea that the creditors have a right to rely upon the fact that the subscribers to such stock have put into the treasury of the corporation, in some form, the amount represented by it; but it does not follow that every creditor has a right to trace each share of stock issued by such corporation, and inquire whether its holder, or the person of whom he purchased, has paid its par value for it. It frequently happens that corporations, as well as individuals, find it necessary to increase their capital in order to raise money to prosecute their business successfully, and one of the most frequent methods resorted to is that of issuing new shares of stock and putting them upon the market for the best price that can be obtained; and so long as the transaction is *bona fide,* and not a mere cover for 'watering' the stock, and the consideration obtained represents the actual value of such stock, the courts have shown no disposition to disturb it. Of course, no one would take stock so issued at a greater price than the original stock could be purchased for, and hence the ability to negotiate the stock and to raise the money must depend upon the fact whether the purchaser shall or shall not be called upon to respond for its par value. While, as before observed, the precise question has never been raised in this court, there are numerous decisions to the effect that the general rule that holders of stock, in favor of creditors, must respond for its par value, is subject to exceptions where the transaction is not a mere cover for an illegal increase."

Parties Interested in Issue of Bonus or Watered Stock. The parties interested in an issue of watered or bonus stock are the corporation, the stockholders, and the creditors. The authorities are agreed that the corporation and all

assenting stockholders are bound by the issue of such stock. The rights of creditors have been sufficiently discussed in the preceding sections.

§ 111. **Fraudulently Issued Stock.** A corporation may issue stock, in excess of the limit fixed by law, intentionally or accidentally. This is invalid, even in the hands of a *bona fide* purchaser for value, and the corporation can have it declared void and cancelled. The possession of certificates of stock representing an over-issue clearly can confer no rights of membership. The amount of capital stock is fixed by the charter of the corporation. A *bona fide* holder of over-issued stock may, however, recover damages from the corporation if its certificates were signed by the corporate officers and when acting within the apparent scope of their power and authority. The corporation is estopped to deny the act of its officers or agents under such circumstances.

§ 112. **Methods of Issuing Capital Stock.** Capital stock may be issued by the corporation in return for money or money's worth, and as between itself and the original stockholder, in the absence of statutory limitations, for an agreed percentage up to and including its par value. Its creditors, however, are not bound by such arrangements, when less than par is paid for the stock. Where the corporation receives cash for the stock issued, no controversy can arise in respect to the sufficiency of the payment. The courts are uniformly agreed, however, that not only may capital stock be issued for money, but also for money's worth, which may consist of property transferred, to the corporation in exchange for the stock, or services, or construction work for and on behalf of the corporation. The claim may be made under such circumstances that the stock thus issued is watered or bonus stock. The value of the services, the property exchanged, or the construction work, in these cases will determine the validity of the transaction. If of a fair and reasonable value at the time of the transaction, and if the parties acted in good faith, the courts have held that the corporation has received its money's worth for

the stock issued. The transaction will, therefore, be valid and the stock not regarded as watered or bonus stock. The question involved, it will be observed, is whether there was a fraudulent overvaluation, and the answer depends upon the facts in each case. If the stock was exchanged for property or construction work, its value at the time the exchange was made determines the rights of the parties, although there may have been a subsequent material and substantial depreciation in the value of the property, or although the construction work may have been done at a much cheaper price later.

Another method by which the corporation may issue stock is through the declaration of a stock dividend. Where this is done, the authority for an increase of capital stock must first exist. If the corporation can legally increase its capital stock, a stock dividend will not be unlawful if the corporation has property equivalent at a reasonable and fair valuation to the par value of the stock then issued and further equal to the increase of its capital stock at the time of the declaration of the stock dividend. It is immaterial to the creditors of the corporation, or the State, whether its entire capital or only a proportion of it is represented by capital stock. The State can only complain where the corporation has violated some express statutory provision. The creditors are only afforded relief when they have been defrauded through the issue of the stock dividend. Stockholders participating clearly cannot complain, and the corporation is estopped to deny the validity of its action.

§ 113. Transfer of Capital Stock. *Right Of.* Shares of stock are personal property and, in common with property of like character, can be transferred freely and at the will of the owner in the absence of express statutory provisions. The right to transfer, it has been held, is of vital importance, since one of the principal reasons for the organization of a corporation and the phenomenal growth of artificial persons in recent years is the readiness afforded to owners of stock to withdraw from the corporation by a transfer of their interest. It has been and is now the policy

of the courts to afford the greatest possible freedom to the owner of personal property to acquire and dispose of the same. The right of transfer is not derived through the charter of the corporation, but is incident to ownership.

Regulation Of. The right of transfer, as already stated, is absolute except when restricted by charter or statutory provisions. The corporation itself has no power to prohibit the transfer of shares, nor is it within the power of the corporation or of the corporate officers or directors to adopt regulations which unreasonably limit the right of the stockholder to transfer his interest in the corporation at will. It has been held, however, in some cases, that where express charter provisions provide limitations upon the power of alienation, these control, since they constitute a part of the contract between the members of the corporation and the corporation. By-laws, or agreements, which place restrictions upon a transfer of shares, will be ordinarily held void as in restraint of trade. This principle does not apply to the power of the corporation to prescribe reasonable rules and formalities to be observed by the stockholder in the transferring of shares, not only for the protection of the corporation, but in a certain and indirect sense for the protection of the stockholder. By-laws, therefore, requiring the surrender of the old certificate of shares of stock to the proper officer of the corporation, for its cancellation before a new one will be issued, have been held valid and not an unreasonable restraint of trade, the certificate of stock being *prima facie* evidence of ownership and the corporation only enabled to determine its membership from an inspection of its corporate records.

Parties Interested in Transfer. The parties directly and immediately interested in a transfer of shares of stock in a corporation are, the corporation, its creditors, the transferor and transferee, and, in some instances, their creditors. The ordinary rule prevails, in the absence of special conditions, that the stock records of a corporation determine, *prima facie,* the relation of the membership in the corporation. To the stockholders belong the right of

voting, of receiving dividends, or inspecting the corporate records, as well as others. They must be notified by the corporate officers of the various meetings of the corporation, dividend checks must be mailed to them, notices of calls or assessments served, and other acts done by the corporation in furtherance of their rights or liabilities as stockholders. It is essential, therefore, that the corporation be accurately informed of its membership. In case of the insolvency of a corporation, its creditors may be entitled, as a matter of law, to enforce their rights, not only against the property of the corporation, but also the stockholders' liability, if any. It is essential, from the creditors' standpoint, that they have accurate information in respect to the corporate membership. As between the immediate parties to the transfer, it is clearly necessary that some record exist which will determine their respective rights and liabilities. It further may be, in some instances, necessary for the individual creditors of the stockholders to attach or reach by due process of law the property of their debtors. Again, the stock records of the corporation must determine who is the stockholder.

Steps in a Legal Transfer. Shares of stock in a corporation, it will be remembered, represent merely the invisible, indivisible interest of the stockholder in the property of the corporation. The written acknowledgment of this interest is the certificate of shares of stock, and the transfer of the stockholders' interest is effected by the transfer of this written representative of his interest. In order to effect a complete formal and legal transfer, which will affect all parties interested in the transaction, certain steps are necessary before the result sought will be accomplished.

The first step necessary is a transfer by *simple delivery,* of the certificate of stock, by the transferor to the transferee, accompanied by a formal instrument of assignment of the stockholder's interest therein, with a power of attorney added. It is usual to have printed upon the back of the certificates of stock this formal instrument, including the power of attorney. When this step is taken, as between

the transferor and the transferee, the transaction is complete. A sale and delivery of personal property, that is, the interest in the corporation, represented by shares of stock, has been effected. The ownership of the property represented by the certificate of shares of stock has passed from the transferor or vendor to the transferee or vendee.

There are other parties, however, interested in the sale and transfer of shares of stock, notably, the corporation and its creditors. Creditors may be entitled to enforce rights against the stockholders and it is necessary for the corporation to determine, at any time, by an inspection of its books, the number of stockholders, their identity, and the amount of interest each has in the assets of the corporation, for the reasons enumerated in the preceding section. To afford the corporation the information and to enable the creditors to ascertain the names of the stockholders, the second and third steps requisite to a legal transfer must be taken, viz, the surrender of the certificate of shares of stock by the transferee to the proper officers of the corporation, its cancellation by them, the issue of a new certificate of shares of stock to the transferee, and, finally, the registration or entry upon the books of the corporation of the transfer of the stockholder's interest from the name of the transferor to the transferee. The courts are uniform in their holding that so far as the corporation itself is concerned, it is only bound to recognize the registered stockholder. Since this is true, it is equally important to the transferee, in order that he may be accorded his rights as a stockholder, that his name must appear upon the records of the corporation as sustaining to it that relation.

"This kind of property, being an intangible right, somewhat akin to the right to receive money due upon a bond or other chose in action, is incapable of actual manual delivery. All that the seller can do that corresponds at all to the delivery of personal chattels in other cases of sale is, to hand over to the buyer his certificate, with a sufficient assignment by deed or otherwise to entitle him to a transfer of the shares on the books of the company. When the

seller has done this, his power and duty in the matter are ended, and it is at the option of the purchaser whether the transfer shall be recorded or not. If the purchaser omits to have the record made, he can claim no rights as a member of the corporation; and he also incurs the further risk of having his title defeated by a subsequent attachment or sale to a *bona fide* purchaser.''[9]

As between the transferor and the transferee, the delivery of the certificate of stock with the assignment is sufficient to convey the legal as well as the equitable title. This assignment may be in blank and the certificate pass from hand to hand, affecting a transfer of the interest in each case. The purchaser, however, cannot claim any rights of membership in the corporation until the final steps have been taken, viz, the surrender and cancellation of the old certificate, with the issue of the new and the registration of his name upon the books of the company.

Forged and Unauthorized Transfers. The universal rule obtains that an owner of personal property cannot be deprived of his interest therein by forgery, theft or otherwise. The rule is also well settled that a *bona fide* purchaser of a negotiable instrument, payable to bearer, although he buys from a thief, acquires a good title if he pays value for it and has no notice of the infirmity of his vendor's title. The statement of these two rules will enable the reader to determine the consequences of a forged and unauthorized transfer of shares of stock. A certificate of corporate shares of stock, it is well settled, in the ordinary form, is not negotiable paper, and the purchaser of such stock, although endorsed in blank by the owner, where no question arises under the by-laws respecting registration, obtains no better title to the stock than his vendor had in the absence of negligence on the part of the owner or his authority to make the sale. On the question of negotiability of a certificate of shares of stock, Judge Comstock, in a New York case,[10] said:

[9] Scripture v. Soapstone Co., 50 N. H. 571.

[10] Mechanics Bank v. R. R. Co., 13 N. Y. 599.

"Such certificates contain no words of negotiability. They declare simply that the person named is entitled to certain shares of stock. They do not, like negotiable instruments, run to the bearer or order of the party to whom they are given."

They are, in some respects, like a bill of lading or warehouse receipt, being merely representative of the property existing under certain conditions and the documentary evidence of title thereto. In an Alabama case[11] it was said:

"The most that can be said is that all such instruments possess a sort of quasi-negotiability, depending upon the custom of merchants and the convenience of trade. They are not, in the matter of transferability protected strictly as negotiable paper."

It will be seen, therefore, that the first rule stated in this section applies and determines the rights of parties where there has been a forged or an unauthorized transfer of shares of stock. The owner cannot be deprived of his property, though his certificate passes into the hands of an innocent purchaser. He may, if he so elects, collect the value of the stock from the corporation, with his damages; but he cannot, on the other hand, if he does not so elect, be deprived of his ownership of an interest in the corporation. These principles apply universally, in the absence of negligence on the part of the owner. This may alter the rights of the parties, as stated above. These rules apply where certificates have been stolen or lost with the owner's name signed to an assignment in blank upon the back thereof, as in the case of a forged signature.

There are many cases where the holder of a certificate of stock endorsed in blank is clothed with power as agent or trustee to deal with such stock to an unlimited extent. It may be transferred in breach of trust or in excess of powers under which the stock is held. It has been held frequently, in this class of cases, that the true owner, having conferred on the actual holder by contract all the external appearances of title and apparently unlimited power of dis-

[11] East Birmingham Land Co. v. Dennis, 85 Ala. 565.

posal, is estopped to assert his title against a third person who, acting in good faith, acquires it for value from the apparent owner. These cases rest upon the principle that it is more just and reasonable, where one of two innocent parties must suffer loss, that he should be the loser who has put trust and confidence in the deceiver than a stranger who has not been negligent in trusting any one. On the other hand, shares of stock may be held in the name of one as trustee, agent, executor, or guardian and there is a sale or transfer for an unauthorized purpose or in excess of the powers conferred. In these cases, the courts have repeatedly held that the true owner cannot be deprived of his property, and may recover damages from the corporation for its loss. The principle controlling here is that where the external appearances exist of a limited or restricted power of transfer on the part of the holder, the corporation is bound to inquire and to satisfy itself of the authority of the trustee or agent to sell and dispose of it.

Effect of Transfer. A transfer of shares in a corporation, when complete, effects a substitution of a new stockholder in place of the outgoing one in the company, and the transferee assumes and acquires all the rights and obligations which attach to the purchaser by reason of his ownership of shares. The transaction involves a novation of the contract of membership. The transferor ceases to be a shareholder in the corporation. He is discharged, ordinarily, from further liability and loses all his right to share in the company's profits or to participate in the management of the corporation. The transferee, on the other hand, becomes the stockholder in place of the retiring member and assumes, impliedly, all of the obligations which rested upon his vendor, and is liable to the extent of the interest in the company which he has acquired.

Lien of Corporation. The absolute right to transfer shares of stock may be limited by statutory provisions granting to the corporation a lien on the capital stock of a member for debts due it by him. In the absence of provisions of this character, a corporation has no lien upon

the stock of a member and cannot prevent a transfer merely because of an obligation due and owing to it from him.

Wrongful Refusal to Transfer. Ordinarily, a corporation has no right to refuse registration to one who presents a certificate of stock for cancellation and the entry of his name upon the books and records of the company. It has been held in some cases, though, that it has the right to refuse to transfer stock to a person *non sui juris,* but it has no right to refuse to transfer stock held by an administrator or other person occupying a trust or a fiduciary relation when the proper authority is shown for the transfer. The same rule is true when applied to dealings by a trustee and sales by a guardian. The corporation may require proof of identity and the genuineness of signatures to the written assignment. The courts go far in holding that it is bound to detect a forgery of the name of a stockholder. It may refuse to transfer stock where it has, by lien or charter provision, a lien upon it for the debts of a member to it, although, in some cases, the transfer may be effected and the stock still subject to the lien. In case of a wrongful refusal, the person presenting the certificate may bring a suit in equity to establish his rights, or may, by *mandamus,* compel the corporate officers to formally complete the registration of the stock presented for transfer; or he may bring an action at law for the conversion of the stock and recover the damages which he can prove he has sustained.

The corporation may lawfully, however, refuse to issue a new certificate, except upon surrender of the old, as required by the by-laws of the corporation. Where it is claimed that a certificate has been lost or destroyed, it is customary for the corporation to require the giving of a bond protecting it against loss in case the old certificate should be presented for transfer. In some States, by statutory provision, it is obligatory upon the corporation, in case of lost or destroyed certificates, to issue a new one after the lapse of a certain prescribed time and without the giving of a bond of indemnity by the one receiving the new certificate.

CHAPTER XIV

SUBSCRIPTIONS TO CAPITAL STOCK

§ 114. Legal Nature of Transaction. A subscription to the stock of a corporation, when accepted, is a contract, and governed by the same principles of law as other contracts. The subscription may be made either for shares of stock in an existing corporation or in one to be organized. The general rule obtains that in the latter case the subscription merely is a continuing offer which may be accepted by the proposed corporation when its organization is complete, but which, until such acceptance, may lapse or be revoked.

"A subscription by a number of persons to the stock of a corporation to be thereafter formed by them has in law a double character. First, it is a contract between the subscribers themselves to become stockholders, without further act on their part, immediately upon the formation of the corporation. As such contract it is binding and irrevocable from the date of the subscription, at least in the absence of fraud or mistake, unless cancelled by consent of all the subscribers before acceptance by the corporation. Second, it is also in the nature of a continuing offer to the proposed corporation which, upon acceptance by it after its formation, becomes, as to each subscriber, a contract between him and the corporation."[1]

In the case of the subscription to the stock of a corporation already formed, the contract, of course, results upon the acceptance of the offer, and the first point to be examined is always as to which party made the offer. If the corporation merely opens books for subscriptions, it is held that the subscriber for shares is the one making the offer, and that the contract does not result until there has been an acceptance on the part of the corporation. But if the

[1] Minneapolis, etc., Co. v. Davis, 40 Minn. 110.

corporation makes a general solicitation of subscriptions, a subscription in accordance with such offer is an acceptance and will result in a contract *ipso facto,* and the subscriber becomes a stockholder by that act and he is bound to pay his subscription. Subscription after the corporation is formed should be distinguished from a sale of shares by it. In the first instance the contract becomes complete upon acceptance, and it is not necessary for the corporation to tender a certificate of stock before taking steps to enforce the subscriber's liability; while in the case of a sale of stock the ordinary rules of sales apply and the certificate must be delivered or tendered.

§ 115. Who May Subscribe. The general rule obtains that anyone who is in law capable of contracting may make a valid subscription to the stock of the corporation, and the ordinary rules regarding infants, lunatics and married women apply in this case as in other contracts. Whether one corporation may subscribe for shares of stock of another corporation already existing or to be formed will depend upon its charter powers to acquire and hold stock in other corporations. The general rule, it will be remembered, is that in the absence of express authority to this effect it cannot be done. A corporation cannot subscribe for its own stock. In general, a subscription made by a duly authorized agent will be valid. The question of the authority of the agent is here the material one, although an unauthorized act of an agent in subscribing for the shares of stock of a corporation may be subsequently ratified by the principal in one or more of the usual ways.

§ 116. Contract for Subscriptions. *Form Of.* At common law, no particular form of contract was required, and any act from which an intention to become a subscriber could reasonably be inferred was sufficient. There is some conflict upon the question of whether a subscription must be in writing, but the better opinion and the great weight of authority is to the effect that an oral subscription to the shares of stock is as binding as one in writing, unless the latter method is required by statute or charter provision.

In making the subscription the weight of authority is also to the effect that mere irregularities and informalities are to be disregarded, and that any agreement showing an intent on the part of the subscriber to become a stockholder in the corporation will be binding. The courts also hold that where one accepts the duties of a stockholder, or claims any of the rights appertaining to that relation, this act will be regarded as tantamount to a subscription to its shares of stock. Illustrations of the application of the principles stated will be found in cases holding that the acceptance and retention of a certificate of stock constitutes one a stockholder. A subscription made in a pocket memorandum book or on a single sheet of paper have been held to effect the same results. On the other hand, the signature of an individual to an incomplete copy of articles of incorporation, to a copy with the names of the directors left blank; where there has been a subsequent alteration of the subscription papers; where the business of the corporation is illegal; or where there is a misunderstanding as to the nature of the paper signed, have been held conditions sufficient to release a subscriber.

Consideration Of. A subscription for shares of stock in a corporation implies a promise to pay for them which sustains an action to collect without proof of any particular consideration. Since a consideration is an essential and material part of a valid contract, the courts have held that in the particular form of contract under consideration, a subscription to the shares of capital stock of the corporation, the consideration moving to the subscriber may consist of the advantages to be derived from membership, the stock to be received, the probable dividends or the assumption of actual obligations. Many courts have also held that a consideration is to be conclusively implied by law from the fact of subscription, and this rule applies to subscriptions taken before as well as after incorporation.

§ 117. Conditional Subscriptions. Subscriptions are sometimes made with some condition attached. These cases will fall into two general classes: subscriptions upon a con-

dition precedent and subscriptions upon a condition subsequent, or, as the phrase is used by many authorities, subscriptions upon special terms.

Conditions Precedent. A subscription to the stock of an existing corporation which is to take effect and become binding only in the event of the performance or the fulfillment of some act, or the happening of some contingency, lawful in itself, provided the corporation sees fit to accept it, is a valid present contract upon condition precedent. Until this condition is complied with, the subscriber does not become a member of the corporation and he is not entitled to any of the rights nor subject to any of the liabilities of a stockholder. If the time is named within which the condition must be performed, the subscription will lapse unless there is a performance within that time. Where the conditional subscription is not valid at the time it is made, because the corporation has no authority at that time to accept a subscription of this character, it may be treated as a continuing offer to subscribe upon the particular conditions, and it will become binding if not withdrawn before the conditions have been complied with. A subscription upon condition precedent to the stock of a corporation to be formed stands upon a different footing and is of doubtful validity. There is no corporation in existence to accept such a subscription and bind the subscriber, and it may operate as a fraud upon other subscribers to the capital stock. As was said by the Supreme Court of the United States:[2]

"The law prescribes that a certain amount of stock shall be subscribed before corporate powers shall be exercised; if subscriptions, obtained before the organization was effected, may be subsequently rendered unavailable by conditions attached to them, the substantial requirements of the law are defeated. The purpose of such a requirement is that the State may be assured of the successful prosecution of the work, and that creditors of the company may have, to the extent at least of the required subscription, the means of obtaining satisfaction of their claims. . . .

[2] 16 Wallace, 390.

If the subscriptions to the stock can be clogged with such conditions as to render it impossible to collect the fund which the State requires to be provided before it would assent to the grant of corporate powers, a charter might be obtained without any available capital. Conditions attached to subscriptions, which, if valid, lessen the capital of the company, thus depriving the State of the security it exacted that the railroad would be built, and diminishing the means intended for the protection of creditors, are, therefore, a fraud upon the grantor of the franchise and upon those who may become creditors of the corporation. They are also a fraud upon unconditional stockholders, who subscribed for the stock in the faith that capital would be obtained to complete the projected work, and who may be compelled to pay their subscriptions, though the enterprise has failed, and their whole investment has been lost. It is for these reasons that such conditions are denied any effect."

The general rule of law is also to the effect that conditions attached to subscriptions must be included in the written agreement. Secret and oral conditions are void and cannot be shown.

Conditions Subsequent. Conditions subsequent or upon special terms are those which contain some stipulation on the part of the corporation which operates, or is supposed to operate, in favor of the subscriber. There is a clear distinction between subscriptions of this class and those noted in the preceding subdivision. In the case of a subscription upon condition precedent, the subscriber does not become a member of the corporation until the condition has been performed. In the case of a subscription upon special terms, the stockholder becomes a member forthwith, subject to all the incidents of membership and the non-performance of the special terms or conditions does not affect his status as a member, though it may render the corporation liable in an action for damages. Whether a condition be "precedent or subsequent" is a question purely of intention, and the intention must be determined by considering not only the words of the particular clause, but also the language of the whole contract, as well as the nature

of the act required, and the subject-matter to which it relates.[3] The courts favor conditions subsequent but not conditions precedent, and it is generally held that subscriptions to the capital stock of a corporation may be conditioned as to the time, manner or means of payment, or in any other way not prohibited by law or the rules of public policy, and not beyond the corporate powers of the corporation to comply with. The condition subsequent also must not operate as a fraud upon other subscribers. In a Tennessee case it was said:

"A subscription upon a condition subsequent contains a contract between the corporation and the subscriber whereby the corporation agrees to do some act, thereby combining two contracts, one, the contract of subscription, the other, an ordinary contract of a corporation to perform certain specified acts. The subscription is valid and enforcible whether the conditions are performed or not. The condition subsequent is the same as a separate collateral contract between the corporation and the subscriber, for the breach of which an action for damages is the remedy."[4]

§ 118. Construction of Subscription to Shares. A subscription to the shares of capital stock is a contract, and the general rules of law applying to the construction of contracts will apply equally to this particular contract. The construction must be reasonable and according to the intent of the parties, and in determining this the circumstances of the subscription are to be considered. It might be said, however, that the courts have adopted one especial rule which is, that that construction of the contract will be followed which facilitates the organization and carrying on of the enterprise, rather than that interpretation of it which would defeat or impair its success. Ambiguities are, in common with other contracts, questions of fact to be determined by a jury.

§ 119. Enforcement of the Contract. A subscription to

[3] Buckport, etc., Ry. Co. v. Brewer, 67 Maine 295.

[4] Maury v. Steel Co., 87 Tenn. 262.

the stock of a corporation implies an agreement, as already stated, to pay therefor, and this obligation may be enforced by the corporation whether it be a subscription obtained before or after incorporation. The manner in which this obligation may be enforced varies. Generally, by charter, the power is conferred upon the corporation to forfeit the shares of the delinquent stockholder, but this power cannot be enforced unless expressly authorized. The right of enforcement must be exercised in a reasonable manner, and statutory provisions, if any, must be complied with. The usual method of enforcing liability is by action on the implied promise, although some States reject the idea of an implied contract, and hold that an action can be maintained by the corporation only in case of an express promise. Unless the statutory method by way of a forfeiture is made exclusive, it is the general rule that the two methods are cumulative, and the corporation may elect which one to pursue.

§ 120. Calls and Assessments. A call has been defined as an official declaration by the proper corporate authorities that the whole or a specified part of the subscription for stock is to be paid. No call or assessment is necessary when, by the charter, or by the terms of the subscription, it is made payable immediately or on or before a date certain. In the absence of provisions of the character noted, and especially when such a proceeding is provided for in the subscription itself, or in the charter or by-laws of the corporation, a call or assessment is necessary to perfect a right of action against the stockholder on his subscription. A call or assessment must be made in the proper manner and by the proper officers, but one is not necessary in cases of corporate insolvency. The stockholders cannot question the advisability of the call, this being a matter which is left exclusively to the official judgment and discretion of the managing officers of the corporation.

Calls or assessments must be uniform and require a proportionate contribution from each subscriber, but where

some of the stockholders have already contributed more than their share, the calls should be directed to those who are in arrears. The call to be effective and to serve, in cases of delinquency on the part of a subscriber, as a basis of action by the corporation against the subscriber, must be certain in respect to the time, the place, the manner in which, and the person to whom is to be paid the sum required by the call to be paid.

§ 121. Defenses. In case an action is brought to enforce the payment of a subscription to the shares of stock of a corporation, the subscriber, as defendant, may interpose as defenses certain facts or equitable rights which, if successfully maintained, will relieve him from his liability. The principal defenses urged by a subscriber are those of parol agreement and of fraud, which will be considered in the following paragraphs. In addition to these the subscriber may interpose as a defense the claim that the enterprise has been abandoned; that material and radical changes in the charter have been made without his express or implied consent; that conditions precedent have been unperformed; and that the corporation, without his consent, has consolidated with others.

Parol Agreement. Where the contract is in writing the defense of parol agreement will not be available to a subscriber to the shares of stock of the corporation. The usual rule applies that oral agreements or conversations are not admissible to vary, alter, or change the terms of a written contract: that neither party will be permitted to prove a different contract from the written one.

Of Fraud. "It is a general rule of law, that, if a person is induced to enter into a contract by false representations, fraudulently made by the other contracting party or his agent, the contract is voidable at the option of the innocent party. This rule applies with full force both to contracts of membership and to contracts to purchase, or to take shares in a corporation at a future time. It may be stated as a general rule, that if a subscription for shares was obtained by fraudulent representations, it may be

annulled by the subscriber at any time before equities have intervened.'"[5]

If the fraudulent representations are made by the promoters prior to the organization of the corporation, the difficulty arises that the promoter is acting for a principal not yet in existence. He clearly has no authority to bind the corporation subsequently formed, and the rule seems to be that whether the subscription is made in good faith or through fraud the subscriber will be bound. His remedy, if any, is against the promoter personally perpetrating the fraud upon him. Where, however, the corporation is organized, if the agent is acting within the apparent scope of his power and authority, his fraudulent acts and misrepresentations will be binding upon the principal, and the subscriber, if he can prove his case, will be relieved of the liability upon his subscription. A fraudulent representation in connection with this subject may be stated as a statement as to past acts or existing facts, or the omission of such statement, which amounts to a fraud on one who, relying thereon, subscribes to the stock of a corporation to his injury. The fraudulent misrepresentation may be made through, or by means of, the prospectus of the company, its official reports made after organization, oral statements made by its authorized agents and also by a suppression of the truth. The misrepresentation may consist in the omission to state a material and existing fact, equally with positive statements of that which is untrue. The general principles of the law of fraud and fraudulent representations apply to subscriptions made to the capital stock of corporations, and the question frequently arises as to whether the representations can be regarded as fraudulent unless they were known to be false by the person or persons making them.

The common rule applies to subscriptions to shares of stock of a corporation, that if a false representation which is material is made by one with no knowledge of its truth or falsity, he is guilty of fraud in a legal sense. A fraudu-

[5] 1 Morawitz on Corporations, § 94.

lent representation consists in the statement of material facts not true, and their legal character is not changed by the condition that the person making them was not aware of their truth or falsity, or made the statement without the intention to deceive. False representations as to the law controlling the rights or powers of the corporation, or affecting the liabilities of the subscriber to its shares, do not afford a basis for relief by the subscriber.

That certain property has been bought by the corporation, when it held merely an option upon it; that a certain amount of stock had been subscribed, when as a matter of fact the total subscriptions were materially less; that the property of the corporation was free from debt, when in truth there were outstanding obligations; and that the corporation was solvent, prosperous, and engaged in the conduct of a highly remunerative business, when the contrary was true, have each been held false representations of such a character as to relieve the subscriber entirely from his liability.

A distinction must be made, however, between statements specifically alleging what does or does not exist, and expressions of opinion as to the prospects or operations of the corporation. The latter class of expressions are regarded as mere matters of opinion and belief, and though exaggerated and illusory will not afford a subscriber relief on the ground of fraud.

"There is no right of action where such representations consist of the expression of mere matters of opinion or belief as to a present fact, or consist of predictions, or expressions of expectation or hope, as to the future operations or success of an enterprise in which the corporation is engaged or proposes to engage. . . . It has been said that any one who looks at the prospectus of a corporation understands that the thing is colored, in the sense that everything is put forward in the most favorable view."[6]

A representation that the corporation would pay as much as twenty per cent in dividends was held to be a mere

[6] Thompson on Corporations, 2nd ed., §§ 721-723.

expression of opinion, and where an officer of the corporation said to the subscriber: "There is a good thing; you ought to go into it; there is some money in it; you may make twenty per cent on your money; you never put your money into any better investment than that," the statement was held insufficient to sustain the charge of fraud.

CHAPTER XV

MANAGEMENT OF CORPORATIONS OFFICERS AND AGENTS

§ 122. Rights of Members. The individual rights of stockholders in a corporation have been sufficiently considered under the chapter relating to the rights of members. Briefly stated, the rule is that they have no power or right after the election of the board of directors or managing officers to participate in the active and immediate management of the business affairs of the corporation. A further suggestion is appropriate in respect to the powers of the majority. The general doctrine obtains that the majority in interest controls the corporation, but this power is not without its limitations, for the courts have held that while no trust relation, in a technical sense, exists as between the stockholders of the corporation, yet the majority cannot so exercise their power as to deprive the minority of their essential rights. The rule is well stated[1] by J. C. Harper:

"The holders of a majority of the stock of a corporation may legally control the company's business, prescribe its general policy, make themselves its agents, and take reasonable compensation for their services. But, in thus assuming the control, they also take upon themselves the correlative duty of diligence and good faith. They cannot lawfully manipulate the company's business in their own interests to the injury of other stockholders. They cannot by their votes in a stockholders' meeting lawfully authorize its officers to lease its property to themselves, or to another corporation formed for the purpose and exclusively owned by them, unless such lease is made in good faith and is supported by an adequate consideration; and, in a suit properly prosecuted to set aside such a contract, the burden of proof showing fairness and adequacy, is upon the party or parties claiming thereunder."

[1] Cook v. Sherman, 20 Fed. Rep. 175.

The broad principles stated in the first sentences of this note have been frequently applied in recent decisions to many acts of the majority resulting in a consequent injury to the minority interests.

§ 123. Directors: General Authority. It is customary for the stockholders of a corporation, in a stockholders' meeting, to elect a board of directors or managing officers to whom is entrusted the immediate power and right of managing and transacting the business of the corporation for and in its name and behalf. A general presumption of authority exists in respect to the validity of their acts. Statutory or charter provisions usually provide for the place of meeting, but in the absence of restrictions there found meetings held elsewhere than at the principal place of business of the corporation, or in the State where the corporation is created, will be legal, and action taken at such meeting binding. It is a common rule of law applying to all representative bodies, that action taken, to be valid, must be had at a meeting of the body in its representative and legal capacity. This rule also applies to meetings of the board of directors. They must meet as a board and transact business in their official capacity before it will be binding upon the corporation or others.

Directors, as a rule, have no implied power to fill vacancies in their number, and their proceedings, meetings, and powers are controlled and regulated by charter provisions and the by-laws adopted by the corporation.

§ 124. Powers and Qualifications. The scope of the power and authority, not only of the board of directors, but also of the officers and agents of the corporation in general, is determined by the objects for which the corporation was created. A corporation is an artificial person and is, necessarily, represented by natural persons acting as its agents on its behalf as their principal. To determine the general scope of their authority, the sources of power of a corporation may be enumerated: the charter of the corporation, including constitutional provisions, general laws relating to a particular class of corporations and the

articles of incorporation; its by-laws; the conduct of the corporation, as evidenced by some special custom followed in the transaction of its business and not contrary to the preceding, or some general business custom or usage adopted by the corporation in the management of its affairs upon which the public acts and of which the courts take judicial notice.

In the general management of the corporate business, and for the purpose of carrying out its legitimate purposes, corporate officers and agents have all the necessary and incidental powers which are fit and appropriate for accomplishing that end. Their authority need not be, in all cases, expressly conferred, but may be implied. All acts within the apparent scope of their power are binding upon the corporation, although it is not bound by an agent's misrepresentation of his authority where the person with whom he is dealing can ascertain, upon reasonable investigation, or where he has actual notice or knowledge of, the actual extent of the agent's authority. The acts of an agent of a corporation, using the term in its comprehensive sense, will be binding upon the corporation, to state the doctrine in another way, when it has clothed him with the apparent authority to do the act; or where it has allowed him, through negligence, to be clothed with the appearance of power. The apparent scope of power and authority, however, extends merely to the supervision and the management of the company's ordinary and regular business. Directors or agents have no implied power to effect a material and permanent alteration of the business or charter of the corporation, increase its capital stock nor sell the corporate property and close out its business. These rights belong, exclusively, to the stockholders or members of the corporation, and express authority must be conferred by them upon the directors to do these acts or others of a similar nature.

Directors are usually required to be also stockholders in the corporation, and other qualifications may be prescribed by the charter or by-laws.

§ 125. Unauthorized Acts, How Ratified. The unauthorized acts of an officer or an agent of a corporation may be ratified by it through acquiescence in the act, by an acceptance of the benefits resulting from its performance, or by a subsequent and formal ratification of it through the conference of express authority. Or, as has been sometimes stated, an unauthorized act may be ratified on the part of the principal by habitual action, recognition or adoption.

§ 126. Delegation of Authority. To the board of directors is entrusted by the stockholders the immediate power of transacting the business of the corporation, and at common law their powers were co-extensive with the corporation. To what extent the law permits a delegation of these powers can be briefly stated. The character of their duties in respect to the exercise of the powers conferred may be designated as discretionary and merely ministerial or mechanical. The principle usually obtains that a board of directors cannot delegate to subordinate agents the performance of their duties of a discretionary character. They must determine the general policy to be adopted by the corporation in the management of its business and exercise personally and in good faith their own best business judgment in directing the affairs of the corporation. They cannot delegate to others, for illustration, the power of declaring dividends or the duty of making calls on subscribers to the stock. On the other hand duties of a ministerial or mechanical character may be delegated by them to subordinate agents or sub-committees. The appointment of agents, the transaction of ordinary routine business, the execution of a deed or of a note, the preparation of reports required by law and the keeping of necessary records are illustrations of acts which may be properly delegated by them to others. There are some authorities, however, which hold that a board of directors may delegate the performance of some of their discretionary powers to an executive committee selected by them from among their number.

§ 127. Relation of Officers and Agents to Corporation. The general rule obtains that the officers and agents of a corporation sustain to it and the stockholders a fiduciary or trust relation. The words trust relation are not, however, used in the technical sense. They are not, strictly speaking, trustees, but merely agents who bear to the corporation, their principal, a relation of trust and confidence.

In a Pennsylvania case,[2] Judge Sharswood said:

"It is by no means a well settled point what is the precise relation which directors sustain to stockholders. They are, undoubtedly, said in some authorities to be trustees, but that, as I apprehend, is only in a general sense, as we term an agent or any other bailee entrusted with the care and management of the property of another."

Some of the authorities hold that the trust relation, using the term in the sense above indicated, is sustained by the officers and directors of the corporation, not only towards the corporation and its members, but also to the corporate creditors.

Corporate Contracts as Affected by above Relation. It follows, from the doctrine as stated in the preceding paragraph, that the contracts and other acts of the corporate officers on behalf of the corporation and with themselves will be closely scrutinized by the courts, and while not void are universally regarded as voidable, even though the act may result in a benefit or advantage to the corporation. The principle or rule of law, which controls not only officers and agents of a corporation but others occupying a fiduciary or trust relation in dealing with the *cestui que trust,* was well stated in an early case in the Supreme Court of the United States,[3] where the court said, in an opinion by Mr. Justice Wayne:

"The general rule stands upon our great moral obligation to refrain from placing ourselves in relations which ordinarily excite a conflict between self-interest and integ-

[2] Spering's Appeal, 71 Penn. St. 11.

[3] Michoud *et al.* v. Girod *et al.*, 4 How. U. S. 555.

rity. It restrains all agents, public and private. But the value of the prohibition is most felt, and its application is more frequent, in the private relations in which the vendor and purchaser may stand towards each other. The disability to purchase is a consequence of that relation between them which imposes on the one a duty to protect the interest of the other, from the faithful discharge of which duty his own personal interest may withdraw him. In this conflict of interest the law wisely interposes. It acts not on the possibility that, in some cases, the sense of that duty may prevail over the motives of self-interest, but it provides against the probability in many cases, and the danger in all cases, that the dictates of self-interest will exercise a predominant influence and supersede that of duty."

The principle applicable was stated in another and controlling authority that no man can serve two masters. In a Wisconsin case,[4] the court said:

"The idea that the same persons can constitute different identities of themselves by being called directors or officers of the corporation, so that as directors or officers they can be private persons, is a violation of common sense."

Acts Merely Voidable. Although the courts adhere, convey or mortgage to or contract with themselves as without variation, to the general principle stated above, yet the facts in each case will determine whether the act of the corporate officers and agents is void or merely voidable. Although the general rule prohibits an officer or director of a corporation from contracting in his official capacity for the corporation with himself in his personal capacity, the act or contract may be accepted by the corporation and the transaction sustained. The Supreme Court of the United States[5] said:

"It can not be maintained that any rule forbids one director among several from lending money to the corporation when the money is needed and the transaction is open and free from blame. No adjudged case has gone so far as this.

[4] Haywood v. Lumber Co., 64 Wis. 639.

[5] Twin Lick, etc., Co. v. Marbury, 91 U. S. 587.

Such a doctrine, while it would afford little protection to the corporation against actual fraud and oppression, would deprive it of the aid of those most interested in giving aid judiciously and best qualified to judge of the necessity of that aid and of the extent to which it may be safely given."

A contract between a corporation and one of its officers or directors which is open and free from fraud and resulting in a benefit or advantage to the corporation, when sanctioned by a majority of the board of directors, exclusive of the one with whom the contract is made, is generally held binding upon the corporation. Where the validity of an act is questioned, under the principles suggested in this and the preceding section, the burden of proof is upon the offending director or officer to show, not only that there was no resulting injury to the corporation, but also the absolute good faith of the transaction. The general rule is applied and can be taken advantage of by a stockholder in those cases where secret profits have been obtained by reason of contracts made by the directors on behalf of the corporation with themselves.

§ 128. Powers of Officers in General. The officers of a corporation are legally its agents and represent it in the transaction of its business. In general, their power and authority is derived from and limited by the sources indicated in section 124. In respect to individual officers or agents, their power and authority is further limited by the nature of the office the duties of which they are performing. The title of the office indicates the character and extent of their powers. The president, for illustration, of the corporation, is its legal and executive head, and the title of that office clearly gives notice to the world of the extent and character of his authority. This will be limited again by the purpose for which the corporation is organized. The duties and the consequent power and apparent authority of the president of a bank would be, in respect to many acts, clearly distinct and different from those of the president of a railway company or a mining company, or a corporation organized for manufacturing or other pur-

poses. The titles given to other officials of a corporation: secretary, treasurer, cashier, general counsel, superintendent, general manager, and others, in each instance convey the extent and nature of their powers and their consequent authority to bind the corporation in the transaction of its business.

The authority of all officers or agents of a corporation to act for and in its behalf may be limited by the by-laws of the corporation. The extent to which restrictive by-laws affect the rights of third parties dealing with the corporation, without notice or knowledge of them, has been considered. The general rule, it may be repeated, obtains that where the officer or agent acts within the apparent scope of his power and authority, limiting by-laws will not relieve the corporation from the consequent results of its agent's acts.

§ 129. De Facto Officers. A *de facto* officer is one who has the reputation of being, and yet is not, a real officer in point of law. His acts, however, are binding upon the corporation when those of the *de jure* officer would have the same result, and the courts adhere to this principle upon the ground of public policy and also of estoppel.

§ 130. Personal Liability to the Corporation of Officers and Agents. The acts of the corporate officers and agents, including directors or managing officers, for and on behalf of the corporation and in its name, necessarily affect the business of the corporation. The value of its property may be impaired or destroyed as a result, or the corporation may become insolvent, in extreme cases, as a result of these acts. Large losses may occur directly attributable to the act of the corporate agent. The question, then, may arise of the personal liability of the agent responsible, to the stockholders of the corporation for the results of his act. This will be determined by a consideration, again, of the nature of the duty which the corporate officer or agent owes to the corporation in the transaction of its business. In respect to the performance of discretionary matters, the common rule obtains, that they are not respon-

sible for losses occurring because of mistakes of judgment. Neither are they liable in the performance of so-called ministerial duties for anything else than gross negligence or for fraud. In other words, the courts have held that corporate officers and agents, so long as they perform the duties devolving upon them and exercise the powers of the corporation in its behalf, in good faith, with honesty and to the best of their business ability, judgment, and discretion, will not be liable for the results of their acts, however disastrous they may be. This rule is especially true of those officers or agents serving without pay. A liability, however, may be created by statute in respect to the negligence or non-performance of acts specifically required to be done.

CHAPTER XVI

FOREIGN CORPORATIONS

§ 131. Definition: The Corporate Domicil. By a foreign corporation is understood one which is created by or under the laws of another State or country, and the subject of the right of these corporations to transact business elsewhere than in the State of their creation, and the power of other States to regulate them, is one of vast importance, since there is scarcely a single corporation that does not extend its business, not only to other States, but to foreign countries.

In an early case in the Supreme Court of the United States,[1] the court in an elaborate opinion by Chief Justice Taney held that a corporation can have no legal existence out of the boundaries of the sovereignty by which it was created. It exists only in contemplation of law and by force of the law; and where that law ceases to operate and is no longer obligatory the corporation can have no existence. It must dwell in the place of its creation and cannot migrate to another sovereignty. The domicil of a corporation is, therefore, indisputably in the State of its creation, but it may, under the doctrine of comity (to be stated hereafter) acquire for certain purposes a domicil in other States. It has also been established that a corporation is not a "citizen" within the meaning of that provision of the Federal Constitution granting to citizens of one State the same privileges and immunities enjoyed by citizens of other States.

§ 132. Doctrine of Comity. In the Bank of Augusta v. Earle case above cited, it was further held by the court that although a corporation must live and have its being only in the State of its creation, yet it would not follow that its

[1] Bank of Augusta v. Earle, 13 Peters 519.

existence could not be recognized in other places, and the fact of its domicil and residence in one State created no insuperable objection to its power of contracting in another, and while it was a mere artificial being, invisible and intangible, yet it was a person for certain purposes in contemplation of law, and that its existence as an artificial person in the State of its creation could be acknowledged and recognized by the law of the nation where the dealing takes place and that it could be permitted by the laws of that place to exercise there the powers with which it was endowed by the charter of its creation. This is, in brief, a statement of the principle or doctrine of comity as applied to corporations. It has been adopted substantially by all the States in the Union, as well as other civilized nations, and it is held to be no impeachment of foreign sovereignty. The adoption of the principle contributes so largely to promote justice between individuals and to produce friendly intercourse between the sovereignties to which they belong, that courts of justice continually act upon it as a part of the voluntary law of nations.

§ 133. Power Of. The doctrine of comity enables a foreign corporation to transact business elsewhere than in the State of its creation, and the question naturally arises as to the extent of its powers when so acting. Judge Story said, upon this question:[2]

"The power of a corporation to act in a foreign country depends both upon the law of the country where it was created and on the law of the country where it assumes to act. It has only such powers as were given to it by the authority which created it. It cannot do any act by virtue of those powers in any country where the law forbids it so to act. It follows that every country may impose restrictions and conditions upon foreign corporations which transact business within its limits."

The power, therefore, of a foreign corporation to act outside of the limits of the State creating it is determined in the first instance by the extent of the powers granted by its

[2] Conflict of Laws, § 106, Note A.

corporate charter and the general law of the corporate domicil and the construction, interpretation and application of the general law of corporations which follows. It is also limited, when acting in a foreign State, by express statutory provisions adopted by that State regulating or limiting the transaction of business by a foreign corporation and by the general public policy of the local sovereign in respect to all corporations, not expressed through specific legislative acts. Ordinarily, a corporation, under the doctrine of comity, is clothed everywhere with the character and powers given by its charter, and its capacity to make contracts elsewhere than in the State of its creation is supported by uniform and long continued practice. While it is true that corporation must "dwell in the place of its creation and cannot migrate to another sovereignty", it may transact business and do such acts in foreign jurisdictions as a natural person might do subject to the limitations and regulations imposed by the sovereign State. In stating the exact extent of the power of a foreign corporation to transact business, a legal author has said:[3]

"The recognition which is by comity extended to foreign corporations does not vest them with an unrestricted faculty of extra-territorial action, even within the limits of their charter powers; while the cases are not uniform on this point, yet the weight of authority seems to be that the company's power in the foreign jurisdiction extends only to those acts which may be done through the mediation of agents. Those corporate acts which must be done by the company itself through the persons of the corporators or stockholders, must be performed where the company has a legal existence. The most obvious of these are meetings for the acceptance of the charter and the organization of the corporation."

§ 134. Right of State to Exclude or Regulate. While the doctrine of comity, viz, the recognition of the laws of a foreign jurisdiction, is universally adopted, yet such recognition is not obligatory. It follows, necessarily, that the foreign state may, as a matter of theory, exclude entirely

[3] Murfree on Foreign Corporations, § 8.

the foreign corporation from transacting business within its limits, or it may adopt such regulations controlling them in the transaction of business within the State as it may elect. The foreign corporation has no absolute right of recognition in another State. It depends for a recognition of its corporate existence, or the enforcement of its contracts, entirely upon the assent of that State. The foreign jurisdiction may restrict the business of a foreign corporation to particular localities, or they may require such security for the performance of its contracts with their citizens as the foreign State deems best for their protection. In respect to the expediency and advisability of regulative measures by foreign jurisdictions, the Supreme Court of the United States[4] held:

"It is not every corporation lawful in the State of its creation that other States may be willing to admit within its jurisdiction or consent that it have officers in them, such as, for example, a corporation for lotteries, and even when the business of a foreign corporation is not unlawful in other States, the latter may wish to limit the number of such corporations or subject their business to such control as would be in accordance with the policy governing domestic corporations of a similar character."

Limitations Upon Right to Exclude or Regulate. The Constitution of the United States, in respect to the matters designated in it, is the paramount and controlling law of the United States, and establishes the rights of all persons and citizens within the limits of its operative effect. To the Federal government, by the Constitution, is given the right to regulate interstate commerce, and the courts have held that regulative provisions as to foreign corporations, passed by the different States, may operate as a regulation of interstate commerce, and therefore be unconstitutional. Provisions for the taxation of foreign corporations have notably fallen within the application of this constitutional grant. In a leading case[5] the Supreme Court of the United

[4] Pembina Mining Co. v. Penn., 125 U. S. 181.

[5] Paul v. Virginia, 8 Wallace 108.

States held that the business of insurance was not interstate commerce, with the consequent result that many laws passed by the different States relative to and regulating the writing of insurance policies by foreign corporations are considered valid unless for other reasons void. The constitutional provision in respect to the abridgment of the privileges or immunities of citizens of the United States has also been invoked, and the uniform holding here is that a corporation is not a citizen within the meaning of the term there used. But it has been held that they are persons within the meaning of the fourteenth amendment, which denies to a State the right to deprive any person of life, liberty, or property, without due process of law, or to deny to any person the equal protection of the laws. The protection of the Federal Constitution has also been invoked in respect to the business carried on by foreign corporations owning and manufacturing articles protected by patents, the sole power to grant which, it will be remembered, rests in the Federal Government. But the courts have held on this point that foreign corporations are not entitled to transact their business in foreign states free from regulative measures.

§ 135. Conditions Imposed. The conditions and regulations imposed by the different States upon foreign corporations desirous of transacting business within their limits are many and differ widely in number and character. Of necessity, the reader is referred to an examination of the laws of each State to determine particular questions involved. It can be said that in main the objects of such regulation are, first, to bring the person of the foreign corporation within the jurisdiction of the courts of the State for the purpose of serving process and enabling citizens of the State to maintain actions in the local courts growing out of their business transactions with foreign corporations; and, second, to afford information of the extent, character, and nature of the powers of the corporation to enable persons dealing with them to act intelligently and with knowledge of their corporate powers.

As illustration of the provisions of the first class might be noted: the appointment of an agent to receive process; a requirement that the corporation shall establish and maintain a known place of business; the waiving of the right granted by the Federal statutes to remove actions from local to Federal courts, and others of a similar character.

Provisions coming under the second class are those requiring the filing of a copy of the charter of the corporation with a designated officer, and, in some instances, the by-laws of the corporation. These regulative provisions and requirements apply only to foreign corporations doing business within the State, and coming within the operation of a specific law. A definition of the phrase "doing business" will be given later.

Waiver of Right to Remove. It is a common condition imposed by a State upon foreign corporations, that before one can acquire the right to transact business within its borders it must waive its right to invoke the jurisdiction of the Federal courts in cases arising out of business transactions within the State. Under the Federal statutes residents and citizens of different States have the right to remove an action brought in a State or local court to the Federal courts on the grounds, among others, of diversity of citizenship. To illustrate, an action, if service of process can be obtained, against a foreign corporation, may be brought by a plaintiff, a resident and citizen of a State in its local courts, against a foreign corporation, a resident and citizen of another State. Under the Federal statutes, and acting within the time designated, the defendant, on account of the diversity of citizenship, would be entitled to remove the case from the State to the Federal court. This right of removal is deemed of great advantage, since the trial of the cause is taken from a local court and jury, likely to be, in many cases, affected by local prejudices and sympathies, to a court not affected by these conditions. On the other hand, the plaintiff may be subjected to more expense in the trial of his cause of action by the removal of

the place of trial to a distance from his residence. Whatever the reasons, the rights of the respective parties have been deemed of material and substantial advantage, and, as already stated, the condition requiring a waiver of the right to remove is one frequently found in the laws of the different States. In respect to the validity of such conditions, there is, naturally, a conflict of decision between the State and the Federal courts, the State courts holding to the validity of such conditions, proceeding upon the reason that since it is only by an adoption of the doctrine of comity that a foreign corporation is permitted to transact any business outside the State of its creation, clearly the State has a right to admit it upon such terms as it may elect to impose. On the other hand, the Federal courts maintain, that in respect to the right of removal the Constitution and laws of the United States are the paramount law, and grant to all citizens and persons within the jurisdiction of the United States the right to have actions, in designated cases, tried by the Federal courts; that waiver of the right will not be binding upon them, and that no State can pass a law which will deprive them of this constitutional privilege and right. The Supreme Court of the United States has repeatedly announced the latter doctrine, while decisions of State courts in general adhere to the legality of this particular condition.

On the question of the right to remove a particular case the decisions of the Federal courts are, undisputably, the controlling authority, and the foreign corporation will be entitled, as a matter of constitutional right, to have the case removed. The State, however, if it so elect, may, because of the non-compliance by the foreign corporation with the condition imposed, viz, the waiver of the right to remove, revoke the license of the foreign corporation enabling it to transact business within the limits of the foreign State and prohibit it from a further transaction of its business there.

Failure to Comply with Conditions. The material question involved is the effect of a failure to comply with condi-

tions imposed upon foreign corporations and which, by the laws of the State, must be complied with before it can have the legal right to transact business within the borders of the foreign jurisdiction. Transactions of a contractual nature comprise the vast majority of the acts of foreign corporations. The general rule seems to be that in the absence of express statutory provisions the contract or the act of a foreign corporation, where stated conditions have not been complied with, are not necessarily illegal and void, but merely voidable. A State may, however, by statute declare results to follow a failure to comply with imposed conditions. The decisions are conflicting, and in the absence of a specific statutory effect they can be roughly grouped into four classes: First, the decisions which hold that foreign corporations can not recover on contracts entered into by them where there has been a failure on their part to comply with statutory provisions relative to the legal transaction of business within the foreign jurisdiction; second, the contracts of foreign corporations are considered as void from the standpoint of the foreign corporation, but not from that of the citizen of the State, who may recover; or, stated differently, the contract is enforcible by the citizen of the State, not by the foreign corporation. This line of decisions, clearly, is not sound. The principle of estoppel should apply equally to both parties to the transaction. Third, a line of cases based in some instances upon express statutory provisions, that failure to comply with conditions merely suspends the right of the foreign corporation to use the remedies and courts afforded by the State to litigants; and, fourth, those decisions, entirely based on statutory provisions, holding to the enforcement of the specific penalty fixed by law for a failure to comply with conditions imposed.

§ 136. **Right to Sue.** The right of a foreign corporation to bring an action for the enforcement of its rights in a foreign state rests entirely upon the principle or doctrine of comity. The right of action is accorded universally, and the doctrine of comity in this respect has been recognized

from the earliest known times. In some States the limitation exists that a foreign corporation cannot prosecute an action in the courts of that State arising out of some act contrary to law or the policy of the State, or which is forbidden by the laws of the State to be done by a domestic corporation.

§ 137. Actions Against. The question of jurisdiction is the primary and essential one under the subject of this section. In many States this is solved by the requirement that, as one of the conditions for the transaction of business within the State, the foreign corporation must appoint or designate an agent or representative upon whom service can be had. The fundamental principle exists and is universally followed that a corporation, the same as a natural person, cannot be sued in an action *in personam* in a State within whose limits it has never been found. The person of a foreign corporation may be, for purposes of jurisdiction, brought within a State other than that of its creation through the appointment, as above suggested, of an agent who stands for and represents the corporation for the purposes specified. Or, it may agree with the State that its person can be regarded as being within the jurisdiction of the State; or, it may agree with the opposite party and appear and defend without raising the question of jurisdiction. Before an action can be maintained and a legal judgment entered against a foreign corporation, its legal person must have been served with process. Where a particular form of service is provided by statute, it is usually regarded as exclusive. Foreign corporations are not domesticated by service of process upon them. Where the foreign corporation complies with the statutory provisions and appoints an agent upon whom service of process can be had, the courts hold that the jurisdiction thus acquired is complete.

Service of Process. The rendition of a legal judgment *in personam* against a foreign corporation is based upon the presence of the person of the corporation within the State. The foreign corporation must be doing business

within the State before any law regulating its business or providing for service of process will be applicable. If service of process is required to be made upon a designated agent of a corporation, compliance with statute will not, *ipso facto,* constitute service upon the corporation. The corporation must be doing business within the State in order to justify service of process against it on its agent. As service of process goes to the jurisdiction of the court over the person, it must be so construed as to conform to the principles of natural justice and so that it will constitute "due process of law". To do this the agent must be one having in fact a representative capacity and derivative authority. The agent must be one actually appointed and representing the corporation as a matter of fact, and not one created by construction or implication contrary to the intention of the parties. The name given to the agent is not controlling. The actual relations of the parties determine his capacity; and, further, the corporation must be doing business in the State and the agent must be transacting the business. The cases all hold that the person served must be an agent of such capacity and authority that in law his presence is the presence of the foreign corporation within the State, and that in law he is, by substitution, the corporation itself. The two questions involved in the service of process upon a foreign corporation are, therefore, first, whether the foreign corporation is doing business within the State; and, second, whether the person served is an agent of sufficient capacity. Otherwise there would be no limit to the right of the State to establish arbitrary rules in regard to service on foreign corporations.

In a leading case in the Supreme Court of the United States,[6] the court said:

"We are of the opinion that when service is made within the State upon an agent of a foreign corporation, it is essential, in order to support the jurisdiction of the court to render a personal judgment, that it should appear somewhere on the record, either in the application for the writ

[6] St. Clair v. Cox, 100 U. S. 530.

or accompanying its service, or in the pleadings or the findings of the court, that the corporation was engaged in business in the State. The transaction of business by the corporation in the State, general or special, appearing, a certificate of service by the proper officer upon a person who is its agent there, would, in our opinion, be sufficient *prima facie* evidence that the agent represented the company in the business. It would then be open, when the record is offered in evidence in another State, to show that the agent stood in no representative character to the company; that his duties were limited to those of a subordinate employe, or to a particular transaction, or that his agency had ceased when the matter in suit arose."

As the service of process involves the constitutional question of due process of law, it is a Federal question, and the decisions of the Federal courts, both in respect to the character or capacity of the agent upon whom process is served, and whether the corporation is doing business, are binding upon the State in construing statutes relative to service on foreign corporations.

Definition of "Doing Business". One of the conditions necessary to obtaining jurisdiction against foreign corporations or the application of laws regulating the transaction of their business, is that it must be "doing business" within the foreign State. This is a question which must be, necessarily, determined by the facts in each particular case, and there are many decisions discussing the question. In one case,[7] the court said:

"A corporation may be servable in a State other than that in which it is organized and incorporated. It must have engaged in business to the extent that it may be said, in legal parlance, to be doing business therein, and the agent served therein must be its authorized representative for the transaction of such business or such as will be deemed generally to represent the company in its corporate capacity."

The act involved in this case was an isolated one, done in connection with a pending law suit, and the court then said:

[7] Ladd Metals Co. v. American Mining Co., 152 Federal 1008.

"But this cannot be considered as doing business here any more than if the defendant had waived the matter of jurisdiction and come into this court to make a defense to the present suit. This also is only a single transaction within itself, and it has nothing to do with the ordinary business of the company. Such a transaction lacks all the features of what is legally denominated doing business with a view of carrying on the business for which the organization was organized and incorporated."

In another case,[8] the court said:

"The question then remains, is the respondent doing business within this State? It seems clear to us that it is not. It is not easy to formulate a general rule by which it can be determined in all cases whether or not a corporation is doing business at a particular place; but it seems to be the consensus of opinion that a corporation, to be within the rule, must transact within the State some substantial part of its ordinary business, continuous in the sense that it is distinguished from merely casual or occasional transactions, and it must be of such a character as will give rise to some form of legal obligation. . . . Merely advertising its business in a State is not doing business within such State."

The question is best illustrated by reference to some concrete cases. The courts have held that the following acts do not constitute doing business within the State by a foreign corporation; an isolated transaction without the intention of continuing business; the single purchase of an article of machinery; soliciting subscriptions to a newspaper published in a foreign state; the sale of goods by traveling salesmen; the frequent purchases of material within a state; the maintenance within a state of an office occupied by persons engaged in advertising and soliciting business for a foreign corporation.

[8] Gaudie v. Northern Lumber Co., 74 Pac. Rep. 1008; see also North Wis. Cattle Co. v. Oregon Short Line R. R. Co., 105 Minn. 198.

CHAPTER XVII

DISSOLUTION AND INSOLVENCY

§ 138. Dissolution: How Effected. The dissolution of a corporation has been defined "as that condition of law and fact which ends the capacity of the body corporate to act as such and necessitates a final liquidation and extinguishment of all the legal relations subsisting in respect to the corporate enterprise." According to the common law and the older textbook writers, a dissolution could be effected in four ways: *First,* by an act of the legislature under a reserved power to repeal; *second,* by death of all its members; *third,* by a forfeiture of the charter; *fourth,* by the surrender of the charter. And to these may be added: *fifth,* by the expiration of the statutory period of its existence; and *sixth,* a compliance with statutory requirements providing for a voluntary dissolution. The manner of and conditions affecting a dissolution, under the circumstances above noted, may be briefly considered.

By Act of Legislature. A corporation may be dissolved by an act of the legislature for a misuse or nonuse of its charter or for any other good and sufficient reason if this power be reserved to the State in the original grant. Where the power to repeal does not exist, the doctrine of the Dartmouth College case obtains in all its force, and no action can be taken by a legislative body dissolving the corporation.

By Death of All Its Members. A dissolution of a corporation can be effected for this cause only in the case of non-stock corporations. It is impossible where a corporation has capital stock, for upon the death of a member his interest passes to his representative, as provided by law.

By Forfeiture of Charter. The grant of the corporate charter is always subject to the implied condition that the

powers and privileges therein granted will not be abused, but courts are generally reluctant to decree a forfeiture of a corporate charter. The act of the corporation upon which is based a proceeding brought by the State for this purpose must be one grave and serious in its character and which directly affects the rights and interests of the public. "The public must have an interest in the acts done or omitted to be done. If it is confined exclusively to the corporation and in no wise affects the community, it should not be considered as of those conditions upon which the grant is made."[9] There must be a clear and wilful abuse or misuse of the powers and franchises of the corporation. The question cannot be raised except in a direct proceeding by the State, since it is the State alone which grants the corporate powers and franchises.

By Surrender of Charter. All the stockholders of the corporation, acting in their corporate capacity, can elect to voluntarily surrender the charter of the corporation and if accepted by the State a dissolution will take place. There must be a formal, solemn act of the corporation, before this can be done.

By Expiration of Corporate Life as Fixed in Charter. The corporation may be also dissolved by the expiration of the time fixed in its charter for its corporate existence. Many of the older corporations were organized with a perpetual charter in the true sense of that word, but for many years it has been customary for States, by statutory provision, to fix a definite period for which corporations could be organized, exist, and transact their business in a corporate capacity. Usually, the expiration of the charter period terminates *ipso facto* the life of the corporation, although in some States, by express provision of law, a *de facto* corporation exists for a designated time for the purpose of winding up the affairs of the corporation, liquidating its debts and distributing its property.

Statutory Methods for Dissolution. The different States now, quite generally, by statute, provide methods for the

[9] Harris v. Ry. Co., 51 Miss. 602.

dissolution and winding up of corporations. This may be done either at the instance of the stockholders or of the State. To legally effect a dissolution in this manner, the parties must act as provided by law.

§ 139. **Effect of Dissolution.** Under the common law the effect of a dissolution was to put an end to the corporate existence for all purposes and destroy its power to act in a corporate capacity. Thereafter, it was held it could neither institute nor defend a suit; make nor take a contract. All its debts and claims were extinguished and all actions by or against it were abated. Under the present rulings of the courts, and by statutory provisions in many cases, the severity of the rule above stated has been materially modified for the purpose of protecting the property of the corporation and the rights of its creditors. While, after dissolution, in the absence of express statutory provisions, it cannot exercise corporate powers, yet its property and property rights are not destroyed. Its rights of action remain, but the remedies are merely changed. The property of the corporation and its rights will be taken in charge by a court of equity; or, if the statutes so provide, by the person therein designated, and managed as a trust fund for the benefit of creditors and of the stockholders. Under these circumstances the closing out of the affairs of the corporation must be as speedily accomplished as possible with the best interests of its creditors and stockholders in view. The obligations of contracts survive, except such as are incapable of specific performance, and the creditor may enforce his claims against the property of the corporation. Executory contracts, as a rule, cannot be carried out. In many cases it has been held that one contracting with a corporation acts upon the implied assumption, in all cases, that its corporate life may be terminated before the contract will be fully performed, and is, therefore, entitled to no further rights under it nor a claim for damages on account of the failure on the part of the corporation to fully perform. This rule, however, does not apply to the voluntary dissolution of a corporation,

for it cannot, by its own acts, relieve itself of its contracts and their obligations.

§ 140. Corporate Insolvency. The insolvency of a corporation does not affect its legal existence, as the possession of property is not necessary to corporate life. Statutory provisions exist in all States providing, in cases of insolvency, for the appointment of a receiver to take charge of the business and property of the corporation for the benefit of its creditors. These provisions are so numerous and involved that no special reference can be made to them that will be of assistance, but, on the contrary, might be confusing. The appointment of a receiver is one of the inherent original functions of a court of equity. The power to appoint a receiver is discretionary with the court, but when done, that officer is regarded as an arm of the court and considered as acting for and on behalf of the court. His possession of the property is held to be possession by the court and interference with it will not be tolerated.

§ 141. Receiver. *Powers Of.* The rights of a receiver of an insolvent corporation are generally limited by the order of appointment. Where this is general in its nature, the receiver is vested with ample authority to conduct the business of the corporation, having in view the speedy adjustment of its obligations. He can originate proceedings looking to the enforcement of the rights of the corporation; employ counsel; make contracts for a limited time in the conduct of the business; purchase property where necessary to carry on its business; compromise claims; and, in general, do all necessary acts in furtherance of the specific objects and purposes for which he was appointed. He is entitled, in the performance of his duties, to the protection of the court, and can, as a matter of right, apply to it for instructions when he deems it advisable.

Duties Of. The duties of a receiver are to obey the orders of the court; to exercise in good faith the powers vested in him by the order of appointment; to be impartial in the performance of those duties and to preserve the property of the corporation.

Liabilities Of. He may be personally liable for using or converting the property of the estate; for his personal dishonesty or misconduct in the management of its affairs; in the personal purchase by him of property of the estate; and he is also liable as representing the estate on contracts in force at the time of the appointment remaining partially unexecuted.

Priority of Claims Against Estate or Receiver. Upon the insolvency of the corporation and the appointment of the receiver, the statutes may prescribe the manner and persons to whom the property of the corporation, as it is disposed of, may be distributed. If no statutory provisions exist in respect to preferred creditors, the court, in its orders from time to time, may establish such priorities or preferences as will accord with established rules and principles of equity. Where an insolvent corporation is, at the time of the insolvency, a going concern, the court usually directs to be paid the claims of those rendering services or furnishing the supplies that enabled it to continue its business. The debts of the receiver contracted by him under express orders of the court, or under his general authority, have, as a rule, priority of payment.

PART II

PUBLIC SERVICE CORPORATIONS
(INCLUDING COMMON CARRIERS)

CHAPTER I

SCOPE OF PUBLIC CALLINGS

It is a general principle of the law, favored both in law and political economy, that every man may fix any price he pleases upon his own property or services; that he may serve one, and refuse another without offering a reason for his preference, or being called under the law to account therefor; that he may charge one person one price, and another in similar situation and circumstances a different price for the same service or thing. The fact that incidental inconvenience or actual loss may result to others makes no difference, subject, however, to the well-known limitation that no person shall so use his property as to deny to others similarly situated equal freedom in the use and enjoyment of their own. This principle applies to all purely private employments alike, whether operated by a single individual, by a partnership, or by a corporation.

§ 1. **Public Employment.** The freedom of choice as to patron and price is in a large measure curtailed and limited in cases where property is so employed that it becomes affected, or impressed with a public interest. This happens when it is put to a use that makes it of public consequence and affects the community at large. When one devotes his property to a use, or engages in a business or employment

in which the law recognizes the public as having an interest, he in effect grants to the public an interest in that use or business, and must submit to be controlled by the public for the common good to the extent of the public interest he has created. He may withdraw in most instances by discontinuing the use, or business affecting the public, but so long as he maintains the use he must render the service and submit to the control. This public interest in the use of property or in an employment arises where because of natural circumstances or the provisions of the law, or both together, the public from necessity must resort to his premises, or make use of his employment for the purposes to which he has devoted his property, so that he has a monopoly or a partial monopoly for such purpose. This monopoly may arise from natural circumstances or the provisions of the law, or circumstances and law together, but if one accepts the monopoly he must submit to a certain degree of regulation and control by the public for its good, both as to patron and price.

Illustration. The facts related by the Supreme Court of the United States in deciding the great case of Munn v. Illinois[1] illustrate well how an apparently private business may grow to such importance as to be of great interest to the public and, therefore, be subject to regulation, both as to service and price by the legislature of the State where it is situated. In that case an act of the legislature of the State of Illinois fixing the maximum rates of storage in grain elevators in the city of Chicago, and other places in the State having not less than one hundred thousand population, was attacked by the elevator and warehouse owners on the ground, among others, that the fixing of the maximum rate of storage charges was such an interference with private property as to amount to a taking of property without due process of law and, therefore, invalid under the Fourteenth Amendment to the Constitution of the United States. In giving the majority opinion of the Court, Chief Justice Waite said:

[1] Munn v. Ill., 94 U. S. 113, (1876).

"That the great producing region of the West and Northwest sends its grain by water and rail to Chicago, where the greater part of it is shipped by vessel or railway to the eastern ports, and to some extent vessels are loaded in the Chicago harbor and sailed through the St. Lawrence River and across the ocean to Europe. The quantity of grain received in Chicago has made it the greatest grain market in the world. This business has created a demand for means by which the immense quantity of grain can be handled or stored, and this means has been found in grain warehouses commonly called elevators, by which the grain is elevated from a boat or car by machinery operated by steam, into bins prepared for its reception, and from these bins by a like process into the vessel or car which is to carry it on. In this way the large traffic in grain between the citizens of the country North and West of Chicago, and citizens of the country lying on the Atlantic coast, passes through the elevators in Chicago. In this way the trade in grain is carried on by the inhabitants of seven or eight great States of the West with four or five States of the East lying on the seashore, and forms the largest part of the interstate commerce in these States. The grain warehouses or elevators in Chicago are immense structures holding from 300,000 to 1,000,000 bushels at one time. They are divided into bins of large capacity and great strength, and are located with the river harbor on one side and the railway tracks on the other; and grain is run through them from car to vessel, or boat to car, as may be demanded in the course of business. It has been found impossible to preserve each owner's grain separate, and this has given rise to a system of inspection and grading, by which the grain of different owners is mixed, and receipts issued for the number of bushels which are negotiable and redeemable in like kind, upon demand. This mode of conducting business was inaugurated more than twenty years ago (prior to 1876), and has grown to immense proportions. The railways have found it impracticable to own such elevators, and public policy forbids the transaction of such business by the carrier; the ownership has, therefore, been by private individuals who have embarked their capital and devoted their industry to such business as a private pursuit. In this connection it must be borne in mind that although there were, in 1874, fourteen warehouses owned by about thirty persons, nine business firms controlled them, and that the prices charged and received for storage were such

as have been from year to year agreed upon and established by the different elevators or warehouses in the city of Chicago, and which rates have been annually published in one or more newspapers printed in said city, in the month of January in each year, as the established rates for the year then next ensuing such publication. Thus it is apparent that all the elevating facilities through which these vast productions must pass on the way to four or five of the States on the seashore may be a virtual monopoly. Under such circumstances it is difficult to see why, if the common carrier, or the miller, or the innkeeper, or the hackney coachman, pursues a public employment and exercises a sort of public office that owners of these elevators do not. They stand in the very gateway of commerce and take toll from all who pass. Their business most certainly tends to a common charge. Certainly, if any business can be clothed with a public interest and cease to be private property only, this has been. It may not be made so by the operation of the Constitution of Illinois, but by the facts. The statutes of the State of Illinois require all railroad companies, receiving and transporting grain in bulk, or otherwise, to deliver the same at any elevator, to which it may be consigned, that could be reached by any track, that was or could be used by such company, and that all railroad companies should permit connections to be made with their tracks, so that any public warehouse might be reached by the cars on their railroads. . . . It is conceded that the business is one of recent origin, that its growth has been rapid, and that it is already of great importance. And it must also be conceded that it is a business in which the whole public has a direct and positive interest. It presents, therefore, a case for the application of a long-known and well-established principle in social science, and this statute simply extends the law so as to meet this new development of commercial progress. It matters not in this case, that these plaintiffs in error had built their warehouses and established their business before the regulations complained of were adopted. What they did was from the beginning subject to the power of the body politic to require them to conform to such regulations as might be established by the proper authorities for the common good. They entered upon their business and provided themselves with the means to carry it on subject to this condition. If they did not wish to submit themselves to such interference, they should not have

clothed the public with an interest in their concerns. In countries where the common law prevails it has been customary from time immemorial for the legislature to declare what shall be a reasonable compensation under such circumstances, or perhaps more properly speaking, to fix a maximum beyond which any charge made would be unreasonable. Undoubtedly in mere private contracts relating to matters in which the public has no interest, what is reasonable must be ascertained judicially, but that is because the legislature has no control over such a contract. So, too, in matters which do affect the public interest, and as to which legislative control may be exercised, if there are no statutory regulations upon the subject, the courts must determine what is reasonable. The controlling fact is the power to regulate. If this fact exists, the right to establish the maximum of charge as one of the means of regulation is implied. In fact, the common-law rule, which requires the charge to be reasonable is itself a regulation as to price. Without it the owner could make his rates at will and compel the public to yield to his terms or forego the use."

§ 2. Test of Public Employment. There is a certain line of authorities based on the same reasoning as the dissenting opinion in the case of Munn v. Illinois,[2] that seems to hold that a business to be subject to regulation by the legislature must require in its prosecution the exercise of some public right granted to it, either as a license or a franchise, such as the use of the public streets and alleys by licensed hacks and draymen, and the exercise of eminent domain by railroads, and the like. But by the better reason and the weight of authority, these privileges are exercised because the person using them is engaged in a public business, and such privileges and franchises can not be legally granted to persons engaged in a purely private enterprise. Such public franchises are granted in aid of the public enterprise. An attempt to grant to one engaged in a purely private business, public rights, such as eminent domain and the right to occupy public streets and alleys, would be a taking of private property for a private purpose, which is prohibited by the Constitution of the United

[2] See *supra*, footnote 1.

States and the Constitutions of the several States. To say that a business is subject to public regulation, because it exercises a public franchise granted to it by the State, is to substitute cause for effect. It is practically impossible to formulate a definition that will include all of the lines of business that have been held to be public employments, subject to regulation by the legislature, and exclude all employments and lines of business that have been held to be purely private callings and, therefore, not subject to such regulation on the part of the public. Thus it is now universally held that the innkeeper and common carrier are engaged in public callings, and have certain public duties to perform which are fixed by the law, but on the other hand it has been held that even in a State where the laws required a physician to obtain a license prior to entering upon the practice of his profession, such physician was not obliged to render service to one requiring it, even though his fees were tendered in advance, and no other physician could be obtained, and such physician being at that time engaged in the active practice of his profession.[3] It would seem that under some circumstances the public welfare would as strongly demand that the members of the community have the services of a physician, as that they be furnished with railroad and telephone facilities.

§ 3. **Elements of Public Employment.** The following elements will be found more or less prominent in public callings that are held by the courts to be subject to regulation by law:

(1) A large demand by the community at large for the article or service furnished.

(2) The furnishing of an article or service, that from its nature cannot well be furnished by a number of firms, or individuals operating separately, so as to create effective competition, either because of the large investment required, or because the public good or convenience demands that the article be furnished, or the service rendered by a single individual, or company.

[3] Hurley, Administrator, v. Eddingfield, 156 Ind. 415, (1901).

(3) Where the delivery of an article or the rendering of a service, necessarily requires the exercise of some public franchise, such as eminent domain or the occupancy of the public streets or alleys of a city or town.

(4) A holding out or offering by the individual or company, to render the service or furnish the article to the public in general, or a contract with the State or community to render the service.

(5) A monopoly in the article or service to be rendered based either on the nature of the article or service, or upon exclusive privileges given by the law, so that individual members of the community are not able advantageously to contract separately for such service.

§ 4. Court Decisions. The following lines of business or occupations have been held to be public employments upon the various grounds indicated: A company engaged in furnishing a town or city with pure water;[4] a railroad company operating a railroad on the ground that railroads have a monopoly of the transportation business, that all the citizens of necessity are compelled to purchase transportation in one way or another, and that in a civilized community freight rates enter into the price of every article in common use; a street railway operating between two points even though built on private property;[5] a cemetery association that sold burial lots for burial of the dead though various sums were charged for burying in different localities, and the cost of such lots was a practical exclusion of some individuals, because the burial of the dead was held necessary to the health of the living and, therefore, a matter of public concern;[6] a log-driving company when granted by law the exclusive right to drive logs in a certain river;[7] a company engaged in furnishing and transporting natural gas, because of the large consumption of gas in the community;[8] companies engaged in the opera-

[4] Lumbard v. Stearns, 4 Cush. 60, (1849).
[5] East Omaha St. R. Co. v. Godola, 50 Neb. 906, (1897).
[6] Evergreen Cemetery Assoc. v. Beecher, 53 Conn. 551, (1885).
[7] Weymouth v. Penobscot Log Driving Co., 71 Me. 29, (1880).
[8] Johnston's Appeal, 7 Atlantic Rep. 167, (1886).

tion by water power of saw and grist mills, because necessary to the welfare and in some instances to the very existence of the community, and because it was necessary to grant to the owners of such mills the right of eminent domain to enable them to obtain the right to construct dams across streams, and dam up water and overflow adjoining lands for the purpose of obtaining water therefrom with which to operate such mills;[9] companies operating grist and saw mills by means of steam engines, because rendering a public service similar to water mills;[10] an irrigation company by analogy to a railroad;[11] a telegraph company on account of the public interest in the business;[12] an electric light and power company because the public interest would be subserved by the use of electricity for light and power;[13] a telephone company as a common carrier of news by analogy to a railroad company; "The Associated Press", organized to buy, gather, and accumulate information and news, and to then supply, distribute, and publish the same, because from the time of its organization and establishment in business it sold its news reports to various newspapers who became members, and the publication of that news became of vast importance to the public, and the operation of such a business required the expenditures of such vast sums of money that scarcely any newspaper could organize and conduct the means of gathering such necessary information as was centered in the association, and no paper could be regarded as a newspaper of the day unless it had access to and published reports from such an association, and for news gathered from all parts of the country the various newspapers were solely dependent on said association, and if they were prohibited from publishing it or its use refused to them their character as newspapers would be destroyed and would soon become practically worthless

[9] State v. Edwards, 86 Me. 102, (1893).
[10] Burlington v. Beasley, 94 U. S. 310.
[11] Sammons v. Kearney Power & Irrigation Co., 110 N. W. 308, (1906).
[12] Dunn v. W. U. Tel. Co., 2 Ga. App. 845, (1908).
[13] Jones v. N. Ga. Electric Co., 125 Ga. 618, (1906).

publications;[14] grain elevators under the circumstances fully recited in the quotation from the opinion of the Supreme Court of the United States in Munn v. Illinois,[15] *supra*; and even in a case where the volume of business of the elevator was small and the elevator did not necessarily constitute a link in the transportation of grain to market;[16] on the other hand it was held by the Supreme Court of Massachusetts that even in time of urgent need, as at the time of the great strike of the Pennsylvania coal miners in 1903, the sale of wood and coal could not be held to be a public business subject to control for the reason that the business of selling fuel can be conducted easily by individuals in competition, and does not require the exercise of any governmental function, as does the distribution of water, gas, and electricity, which require the use of the public streets and the exercise of the right of eminent domain; that it was not important that the sale of coal should be conducted as a single large enterprise with supplies emanating from a single source, as is required for the economical management of the kind of business last mentioned. It did not even call for the investment of a large capital but could be conducted profitably by a single individual of ordinary means,[17] a stock-yards company where the tracks of all principal railroads in that part of the country unite, and stock raisers meet and deal with packers and purchasers of live stock, and because of the nature of the business and the railroad facilities the establishment of other markets was impracticable, thus making the stock yards of necessity the only available place for breeders, feeders, and dealers in live stock to meet and market their stock, such company thereby having a practical monopoly of a vast business affecting thousands of people;[18] a terminal company which had voluntarily devoted itself to furnishing passenger terminal facilities

[14] Inter Ocean Pub. Co. v. Assoc. Press, 184 Ill. 438, (1900).

[15] People v. Budd, 117 N. Y. 1, (1889).

[16] Brass v. N. Dak., *ex rel.* Stoeser, 153 U. S. 391, (1894).

[17] Opinion of Justices, 182 Mass. 505, (1904).

[18] Ratcliff v. Wichita Union Stock Yards Co., 86 Pac. Rep. 150, (1906).

to railroad common carriers;[19] the Board of Trade of Chicago, because it furnishes market quotations that are clothed with a public interest and must, therefore, furnish reports and quotations to all;[20] innkeepers, because necessary for the protection of travelers from inclement weather and highwaymen.

Grounds of Court Decisions. The reasons for holding some of the above callings to be public callings subject to legal regulations have disappeared because of the changes that have come about with the lapse of time, but the courts have still clung to their policy of holding them to be public callings. In most communities it cannot be said that there is now any real necessity for the law controlling the business of an innkeeper, any more than that of a drygoods merchant or any other mercantile business. The retention of the rule, after the failure of the original reason assigned for it, is well illustrated by the laws enacted in many of the States fixing the maximum charge of grist and saw mills originally based upon the necessity of such mill owners, when the mill is to be operated by water power, exercising the power of eminent domain to obtain the necessary water from streams, and the right to overflow lands to obtain water power, but the Supreme Court of the United States held, after the use of steam became common as a propelling power, that such mills operated by steam were still public callings subject to regulation.

§ 5. "Holding Out" Fixes Nature and Limits of Business. A company or individual may engage in a public employment or not as it chooses. One becomes subject to control of the public by engaging in a business in which the public has an interest. Such a company is generally bound to render service only of the kind that it holds itself out and offers to render. The holding out fixes the nature and limits of the business. Thus it was held in the case of Ingate v. Christy,[21] that one who has a counting house and

[19] State v. Jacksonville Terminal Co., 41 Florida 377, (1900).

[20] Stock Exchange v. Board of Trade, 127 Ill. 153; American Live Stock Commission Co. v. Chicago Live Stock Exchange, 143 Illinois 210.

[21] Ingate v. Christy, 3 Car. & K. Q. B. 61, (1850).

was the owner of a lighter and had the name "lighterman" on the doorpost, was a common carrier. A person at common law was a common carrier of just such articles as he chose to be, and no other. If he held himself out as a common carrier of silks and laces, the common law would not compel him to be a common carrier of agricultural implements or other articles. In the case of Faucher v. Wilson,[22] one engaged in the business of trucking goods for hire from a railway freight station to different stores in the city was held to lack the distinguishing characteristic of a common carrier, namely, that of holding himself out as ready to carry for all persons such commodities as were in his line of business. One who holds himself out to the public as engaged in the business of keeping a house for the lodging and entertainment of travelers, for a reasonable compensation, is an innkeeper, but if he only occasionally entertains travelers for compensation when it suits his pleasure to do so, and does not hold himself out to the public as keeper of a house for the accommodation of the traveling public in general, he is not burdened with the duties and liabilities placed upon innkeepers by the law.[23] A company that is engaged in furnishing electric lights cannot be required to furnish gas; neither can a company engaged in supplying a city with natural gas be required to furnish artificial gas, or vice versa.

Manner of Holding Out. This holding out may arise by the company actually engaging in one of the lines of business known as a public calling, and placing itself in a position to render such service. The mere acceptance by a water company of a franchise authorizing it to exercise the power of eminent domain, and the placing of its mains and pipes in the streets and alleys of a city without any express provision in its charter, or in the ordinances of the city permitting it to occupy its streets and alleys, requiring it to furnish water, has been held to be a sufficient holding out to the public for furnishing water, to make the

[22] Faucher v. Wilson, 68 N. H. 338, (1895).
[23] Howth v. Franklin, 20 Tex. 798, (1858).

company bound to serve all citizens of such city without discrimination.[24] Upon principle, and by the weight of authority this is all that is required to place upon such a company the duty of serving the public without discrimination, but the holding out is usually made more explicit and the duties of service more definite by an express contract entered into with the city or municipality whereby in consideration of the grant to such a company, by the State or municipality, of the right to use and occupy its streets and alleys, the company agrees to furnish public service of a particular kind to the city and its inhabitants.[25] There are a few cases holding that such an express contract, or charter provision requiring it, is necessary to enable the courts to compel such a company to furnish service to all, without discrimination. In the case of Paterson Gas Light Company v. Brady,[26] it was held that a complaint that merely alleged that a gas company had laid its pipes in the streets and alleys of a city, but failed to allege the company was holding itself out to persons occupying buildings abutting on the streets where such pipes were laid, or that there was a provision of the company's charter requiring it to render such service, was insufficient to show a duty on the part of the company to render service to all who might apply. This case practically ignores engaging in the public business as an element in subjecting a company to the duties imposed upon public service companies by law.

Under such a rule, if generally accepted, the law could not have made such great strides and arrived at its present efficiency in protecting the interest and welfare of the people at large. The application of the rules relative to public employments could not have been extended to grain elevators, stock-yards companies, and other companies of like kind that do not necessarily require the grant of any public franchise to enable them to prosecute their

[24] Lumbard v. Stearns, 4 Cush. 60, (1849).
[25] Haugen v. Albina Light & Water Co., 21 Ore. 411, (1891).
[26] Paterson Gas Light Co. v. Brady, 27 N. J. Law, 245, (1858).

business, if such a narrow basis for the rules had generally prevailed.

§ 6. Development of Principles. Very early in the history of the law the principle, that the public had an interest in certain employments was recognized by the courts, and rules were established having as their basis the principle that one engaged in such a business must serve all alike who were similarly situated, and must not discriminate in favor of nor against any, and that he must limit himself to reasonable compensation.[27] The rules and principles applicable to such employments have not been confined in their application to the instrumentalities of commerce or to the particular kinds of service known and in use at any fixed time, but the courts have extended their application to keep pace with the progress of the country, to the new developments of time and circumstances. Their application has been extended from the horse with its rider to the stagecoach, from the sailing vessel to the steamboat, from the coach and steamboat to the railroad, from the railroad to the telegraph, and from the telegraph to the telephone, as these new agencies have been successively brought into use to meet the demands of increasing population and wealth. These principles have been established and declared by the highest interests of the country. They are for the government of the business to which they relate at all times and under all circumstances, and no statute is necessary to authorize the courts to enforce them against any person or company who undertakes to supply a demand which is affected with a public interest.[28]

§ 7. Duty to Serve Public. All public service companies must render service to all persons desiring it on equal terms and without discrimination, and for reasonable compensation. If this were not so and if companies, existing by the grant of public franchises, engaged in supplying the great conveniences and necessities of modern life, such as water, gas, electric lights, street cars and the like, could

[27] Allnutt v. Inglis, 12 East 527, (1810).

[28] State *ex rel.* Wood v. Consumers Gas Trust Co., 157 Ind. 345, (1901).

charge any rates they chose, however unreasonable, and could at will favor certain individuals with low rates and charge others high rates or refuse them service altogether, the business interests and the domestic comfort of every one would be at their mercy. They could kill the business of one, and make prosperous that of another, and instead of being public agencies created to promote the public comfort and welfare, these corporations would be masters of the cities and towns they were established to serve. A few wealthy men might combine and by threatening to establish competition with such a company already in existence, procure very low rates for themselves which the company might recoup by raising the price to others.[29]

A natural gas company organized by the citizens of a city for the purpose of supplying gas to the citizens thereof at cost, had entered upon its duties and laid pipes in the streets and alleys of the city. A citizen owning property abutting upon one of the streets where such pipes were laid applied to the company for permission to connect her house with the lines of the gas company for the purpose of using gas, and the company answered that it was not organized for the purpose of making money, and that it was then unable to supply its customers that were already connected with its lines with a sufficient quantity of gas in cold weather, and the court held that since the street in front of applicant's house had been dug up and her property made servient to the use of the gas company in laying its pipes and carrying on its business, that her right to use the gas and share in the public benefit thus secured, whatever it might amount to, was equal to the right of any other inhabitant of the city, and that the right to gas was held in common by all those abutting on the streets where its pipes were laid, and that the legislature could not grant the power to use the city streets for the purposes in which it was used for the benefit of any part of the public less than the whole; that the gas company's contract with the State and its extraordinary powers were granted in con-

[29] Griffin v. Goldsboro Water Co., 112 N. C. 206, (1898).

sideration of its engagement to bring to the community a public benefit, and that there can be no such thing as priority or superiority of right among those who possess the right in common; and that the gas company found it impossible to procure enough gas to fully supply all, was not sufficient reason for permitting it to say that it would deliver all it had to one class to the exclusion of another in like situation. The objection alleged by the gas company was that it had exhausted every available means for increasing its supply of gas, and that it was unable to do so, but it was held that the principle, that mandamus will not lie to require an attempt to be made to do a thing shown to be impossible did not apply to the case for the reason that the applicant was not asking that the company be made to increase its supply of gas, but was only seeking to be permitted to share in the quantity of gas, whatever that might be, that the company had at its command, on the same terms that others were permitted to use it.[30]

It makes no difference whether the party engaged in a public employment is a corporation, a partnership, or an individual, the duty to serve the public is the same. It is the nature of the service under demand that creates the duty to the public, and in which the public has the interest, and not simply the body that undertakes the service.[31] If a person or corporation is in possession of a public franchise, for the grant of which the discharge of any public duty in the way of rendering a public service of any kind was assumed, so long as the franchise is retained such person or corporation will not be allowed to urge as an excuse for failure to perform any duty required of it that it would be unprofitable. It cannot consistently keep the franchise and refuse to perform the duties incident thereto, for the mere reason that such performances would be unremunerative. If the rights, privileges, and franchises granted by the charter are, in connection with correspond-

[30] State *ex rel.* Wood v. Consumers Gas Trust Co., 157 Ind. 345, (1901).

[31] Chesapeake & Potomac Telephone Co. v. B. & O. Telegraph Co., 66 Md. 399, (1887).

ing duties thereby imposed, no longer desirable, the company should simply surrender the charter.[32]

§ 8. Public Service Corporations Are Trustees. It is a firmly-established rule that where one person occupies a relation in which he owes a duty to another, he shall not place himself in any position which will expose him to the temptation of acting contrary to that duty, or bring his own interests in conflict with his duty. This rule applies to every person who stands in such a situation that he owes a legal duty to another, and courts of equity have never fettered themselves by defining particular relations to which alone it will be applied, for they have applied it to agents, partners, guardians, executors, administrators, directors, and managing officers of corporations as well as to trustees, but have never fixed or defined limits. The rule is founded upon the plain consideration, that the one charged with the duty shall discharge that duty, and he will not be permitted to expose himself to temptation or to be brought into a situation where his personal interests conflict with his duty. Courts of equity have never allowed a person occupying such a relation to undertake the service of two whose interests are in conflict and then endeavor to see that he does not violate his duty, but they forbid such a course of dealing, irrespective of his good faith or bad faith. In application of these principles to public service corporations it has been held that the owners of public warehouses may be prohibited from entering into the business of buying and selling grain and storing the same in their own warehouses, because such warehouses are public agencies, and their owners pursue a public employment, and that by buying and selling through their own elevators, the position of equality between them and the public, whom they are bound to serve, is destroyed. Warehousemen storing grain in their own elevators were enabled to overbid other grain dealers by charging them the established rate for storage, while they give up a part of the storage charges when they buy and sell for themselves. A ware-

[32] Savannah & Ogeechee Canal Co. v. Shuman, 91 Ga. 400, (1893).

houseman might overbid other dealers as much as a quarter of a cent per bushel and immediately resell the same to a private buyer at a quarter of a cent less than the grain cost him, and charge storage in an amount more than covering the loss. Further, all the grain coming to warehouses is mixed and graded and warehouse receipts issued to the owners, and the different grades differ in price sometimes to the amount of two cents per bushel; if the warehouseman owns wheat in his own warehouse and issues warehouse receipts to himself, he may manipulate the wheat so as to give himself an advantage in the grade of wheat covered by his warehouse receipt.[33]

§ 9. **Public Duty Not Defeated by Contract.** Such companies cannot avoid or relieve themselves from their duty to serve the public by entering into special contracts to serve one, to the exclusion of others. An irrigation company was held to be a quasi-public corporation and bound to furnish water from its canal on equal terms and without discrimination to all, and a contract entered into by it with another company for the sale of water which provided that said irrigation company should not sell water to any other company intended to compete with such purchaser in the generation of electricity for sale was held invalid, because in violation of the irrigation company's public duties,[34] and this right cannot be defeated by contracts entered into between third persons. A grant by a land company to an oil transportation company, of the exclusive right of way and privilege of laying pipes for transportation of oil over and across a 2,000-acre tract of land, was held not to defeat the right of another company engaged in the same business to obtain such a right of way by condemnation proceedings under the power of eminent domain granted to such companies by the State legislature.[35]

§ 10. **Agreements Destroying Competition.** Where two companies in the same kind of public business are operat-

[33] Cent. Elev. Co. v. People, 174 Ill. 203, (1898).

[34] Sammons v. Kearney Power & Irrigation Co., 110 N. W. 308, (1906).

[35] W. Va. Trans. Co. v. Ohio River Pipe Line Co., 22 W. Va. 600; same case 46 Am. Rep. 527.

ing in the same town or municipality, their duties to the public prevent them from entering into any kind of agreement that they will each refrain from serving the other's customers. Where a gas company had been organized and equipped and was engaged in furnishing gas to the citizens of a city, and thereafter another gas company was organized and obtained the grant of a franchise and was engaged in furnishing the inhabitants of the city with gas, and a contract was entered into between the two companies whereby they fixed the rates to be charged by each of them to a consumer, and further agreed that neither of them would attach service pipes to the house of any gas consumer who was at such time a consumer of the other company; it was held that such agreement was a violation of the duties of such gas companies to serve the public and that the agreement was, therefore, void.[36] Where a telephone company entered into an agreement with the owner of a grocery store, whereby the groceryman agreed not to use the telephone of a rival telephone company, and the groceryman thereafter began the use of the other telephone company's phones, it was held that the first telephone company could not enforce its agreement by taking out its phone.[37]

§ 11. Patented Devices. The grant of a patent by the United States government ordinarily gives the patentee the right to control the use, manufacture, and sale of such devices and determine whether or not any use, or what use, shall be made of the patented invention. He may ordinarily fix the selling price of the article and the price that shall be paid for its use at any amount he sees fit, but if the owner of the patent uses his device in the public service or grants the use of it to a company engaged in one of the employments in which the public has an interest, he loses his absolute right of control. The legal duty which a public service corporation owes to the public is paramount to the inventor's right to control, and the patented invention

[36] State *ex rel.* Snyder v. Portland Nat. Gas & Oil Co., 153 Ind. 483, (1899).
[37] State *ex rel.* Gwynn v. Citizens' Telephone Co., 61 S. C. 83, (1901).

cannot be used as an excuse to withhold from one citizen a public service given to another, nor serve as an excuse to discriminate between individuals.[38] In a case where an electric light company operating in a village had the exclusive right to use certain patented lamps and attachments, and the village by ordinance required a railroad company to maintain lights at its street crossings of the kind that was being used by said electric light company, it was held that since the electric light company was using the streets and alleys of the village for carrying on its business, that it was, therefore, bound to submit to regulation by the public and could not arbitrarily fix the prices that it would charge for lights, and that, even though such electric light company had the exclusive right to use such patented lights and attachments within the village, it was bound to furnish lights to all its customers on terms that were reasonable, and that the railroad company was bound to comply with the ordinance and obtain the lamps, and that its right to be free to contract with whom it saw fit for such lamps must yield to that extent to the police power of the State.[39]

§ 12. **Right of Public to Courteous Treatment.** Public service companies are bound to furnish to such members of the public as have occasion to transact business with them in regard to the service they are holding themselves out to the public to render, safe and decent access to places opened up for the transaction of such business. This duty is not discharged by merely furnishing a place physically safe and free from obscenity, but the customers are entitled to be protected from abuse, humiliation, insult, and other unbecoming and disrespectful treatment. Members of the public are not to be deterred from transacting business with such companies by reason of the fact that they cannot enter their public offices without being subjected to insult or personal affront. And the agent or servant of a customer transacting such business is entitled to the same protec-

[38] People *ex rel.* Postal Tel. Co. v. Hudson River Telephone Co., 19 Abb. N. C. 466, (1887).

[39] Cinn., Ham. & Day. R. R. Co. v. Village of Bowling Green, 57 Ohio State 336, (1879).

tion as the party himself.[40] Not only are customers transacting business with such companies entitled to courteous treatment from the agents and employes of such companies, but they are in general entitled to the same protection from others who may happen in or about the place where such business is to be transacted.[41]

§ 13. Public Service Companies Entitled to Reasonable Compensation for Service. In cases where it is practicable they may require payment in advance in a reasonable amount and refuse to serve those who refuse to pay in advance as required. Thus it has been held that a requirement that a citizen shall pay a water company in advance for a quarter of a year for a supply of water for domestic purposes, and that payment be made in advance for water for sprinkling purposes for a fixed season of seven months, are reasonable requirements.[42] Where one who was a transient in a town tendered a message to a telegraph company that required an answer, and the telegraph company refused to transmit the message and informed the one offering the message that the company had a rule that transient persons sending messages which required answers must deposit an amount sufficient to pay for ten words, and that the amount required to be deposited on the offered telegram was twenty-five cents, it was held that such a rule was a reasonable requirement, and the court said that a person who sends another a message and asks an answer, promises by fair and just implication to pay for transmitting the answer, that it was not unnatural, or unreasonable, or oppressive for the telegraph company to take fair measures to secure payment for services rendered, and that such a rule was fair and reasonable.[43] But rules requiring payment in advance or that security be furnished for service, must be uniform and general in their application to all members of the community. In a case where a gas light and electric company demanded of a citizen a deposit of

[40] State *ex rel.* Gwynn v. Citizens Telephone Co., 61 S. C. 83, (1901).
[41] Batton v. So. and No. Alabama R. R. Co., 77 Ala. 591.
[42] Harbison v. Knoxville Water Co., 53 S. W. Rep. 993, (1899).
[43] W. U. Tel. Co. v. McGuire, 104 Ind. 130, (1885).

twenty dollars as security for the future consumption of gas and electricity and upon his refusal to comply the company withdrew its pipes from his building, it was shown that the company had no general rule requiring such payment in advance and, therefore, had no right to enforce such payment. The court said that the company had no power capriciously, to make special rules to apply to some customers or to a certain customer, and not to others.[44] It has been held that a gas company furnishing a hotel with gas could impose, as one of the conditions required of the owner, that he give sufficient security that he would pay its bills and comply with its regulations, and that the demand of a deposit of one hundred dollars was not unreasonable where the bills of the hotel amounted to fifty and sixty dollars per week.[45]

§ 14. Right to Refuse Service When Former Bills Are Unpaid. Such a company may generally refuse to render service when its former bills remain unpaid. In a case where one had been taking gas from a company and had paid his bills for a while, and then failed to pay certain bills and a judgment was taken against him on the account, and he subsequently applied for gas, and the company furnished him with gas for a while and then demanded the payment of the judgment, and the customer refused, alleging his insolvency, it was held that the gas company had a right under such circumstances to refuse to furnish him with gas any longer, but it seems that where there is a *bona fide* disagreement between customer and company about the payment of a bill, the company will not be permitted to compel its payment by refusing to render the service. In a Nebraska case a telephone company furnished a customer a telephone but failed to furnish him a directory, which the customer claimed was essential to the profitable use of the telephone and which it was the custom of the telephone company to furnish to its subscribers. Finally, but after considerable delay, the

[44] Owensboro Gas Light Co. v. Hildebrand, 42 S. W. Rep. 351, (1897).
[45] Williams v. Mutual Gas Co., 52 Mich. 499, (1884).

directory was furnished, but on pay day the customer refused to pay for the use of the telephone during the time the telephone company was in default with the directory. The telephone company thereupon removed the telephone, and shortly thereafter the customer applied to the telephone company to become a subscriber and have an instrument placed in his place of business, and the telephone company refused to do so. On this state of facts it was held that if the customer was indebted to the telephone company for the use of its telephone, the law gave an adequate remedy by an action against him for the amount due, and that the mere fact of a misunderstanding with one who desires to receive the public benefit derived from the services of the company would not relieve the company from the discharge of its duty to furnish service.[46] It has been held that a requirement that an owner of real estate shall sign a contract making unpaid water bills a lien on his real estate is invalid, and that the failure of the owner of real estate to sign such a contract could not be used as an excuse for the refusal on the part of the water company to furnish water to a tenant of such owner.[47]

§ 15. Power to Make Rules. One of the inherent and incidental powers of all public service companies is the right to make rules for the regulation of their business. Such rules to be valid must be reasonable. They cannot fix a variety of prices or impose different terms and conditions according to their caprice or whim. They may, however, fix reasonable rules and regulations applicable to all consumers alike. In determining the reasonableness of such rules, compactness of the population of the city and various elements composing such population must be taken into consideration. Such a company has no right to base a rule upon the theory that the population of the whole community is dishonest, but it has the right to adopt a rule which gives the honest citizen what he pays for and prevents the dishonest from getting what he never paid for.

[46] State v. Neb. Telephone Co., 17 Neb. 126, (1885).

[47] State *ex rel.* Milstead v. Butte City Water Co., 18 Mont. 199, (1896).

In making rules the board of directors have a right to take into consideration the security and convenience of the company, as well as the right of the public, to be served without unreasonable exaction. It has been held that a water company may make regulations requiring an examination of meters in houses at reasonable times; that it may require that customers shall keep their faucets closed when not using water, and that it may cut off the water service from one who unnecessarily wastes water.[48] Such a company may fix by rules the hours for sprinkling and the kind of apparatus to be used for such purposes; and may require sprinkling devices to be disconnected from hydrants before furnishing water connections in cases where customers do not contract for water for sprinkling purposes.

Rules Classifying Charges. Rules may be established fixing different charges for service based on reasonable differences in service required. At common law whether or not a difference in treatment accorded to different patrons amounts to discrimination, depends upon surrounding circumstances.[49] A mere difference in the amount of the charge does not necessarily constitute unlawful discrimination. Such a corporation has the right to charge a smaller rate to persons who consume a large quantity of their product, such as water, gas, or electricity, than it charges to customers whose consumption is small.[50] Such a company is not bound in the absence of statutory requirements to treat all patrons with absolute equality. It is required to furnish service at reasonable rates, without unjust discrimination. It has been held that a gas company may lawfully adopt a rule requiring persons using or desiring to use gas furnished by the company within said city, to pay a monthly rental for the use of the meter furnished by the company of the sum of a dollar and a quarter per month, providing that in all cases where the consumer used less than five hundred feet of gas, such

[48] Harbison v. Knoxville Water Co., 53 S. W. Rep. 993, (1899).
[49] Snell v. Clinton Elec. Light, Heat, & Power Co., 196 Ill. 626, (1902).
[50] Silkman v. Water Commissioners, 152 N. Y. 327, (1897).

rental was to be in full payment for such gas, not to exceed the amount of five hundred feet in one month. The court supported its ruling by the following reasoning: "It is a matter of common knowledge that to furnish gas at hand for a very small or nominal consumer requires the same outlay in the way of periodical meter inspection, repair, and weekly or monthly visits that are required for very large consumers. The same investment and the same care and oversight is required where the gas consumed monthly will not exceed ten cubic feet, or even one cubic foot, as where the amount may be ten thousand cubic feet."[51] By like reasoning a rule of an electric illuminating company providing for a certain rate of payment for electric current, and fixing a minimum charge which should be paid for each separate month during which the agreement should be in effect, was held to be reasonable. The court in its opinion said that if the customer does not bind himself to use any particular amount of light, the return of the company based on actual consumption would rest merely upon the consumer's volition. It would further depend upon him whether the service he has required of the corporation that it be in constant readiness to render, is profitable or unprofitable to the company; but this constant condition of readiness is a necessary and unavoidable obligation, which must be sustained in order to meet instantaneously the demand for light which the consumer is entitled to have at any moment he wishes it. It thus forms a part of the service to be rendered and is an item properly to be considered, when the reasonableness of the charges exacted by the company is called in question. There having been no price fixed by the legislature, the only condition affecting the charge is that the compensation must be reasonable, and what is also incidental to this requirement that it should be uniform, namely, the same for all consumers similarly situated. The charge the company makes is based primarily upon the actual consumption,

[51] State *ex rel.* Weise v. The Sedalia Gas Light Co., 34 Mo. App. 501, (1889).

over which it has no control. One consumer with the same number of lights will use more than another. In both cases the return may be remunerative, but the use of one may be so inconsiderable as to involve a loss. To meet this contingency a monthly minimum charge was made. This payment is not in addition to the charge for actual consumption, because where light is consumed which entitles the company to payment on meter measurements of a sum per month, equal to or greater than the minimum charge the consumer pays only for the light he has actually had. The minimum charge fixed is not a penalty for failure to use the light, but it is properly regarded as compensatory, therefore, reasonable.[52]

And further, in a case where a gas light company had been supplying a citizen, but the citizen had used electric lights almost exclusively and had made but very little use of the gas, except as emergency light when for one cause or another he was not supplied with electricity; and when the citizen applied for gas connections, the gas company refused to make them unless he paid fifty cents a month as meter rent; it was held that the meter rent was a proper charge even though it was not shown that the gas company had any other consumer who used its gas for a like purpose and it was shown no other customer was charged meter rent,[53] and it has been further held that under such circumstances the company could refuse altogether to furnish service.[54]

Such companies are not bound to uniform charges for service except in the district where it exercises its franchise rights and holds itself out to render service. In a case where a telephone company had been operating a local telephone system in and around a city for a period of about seven years and had four hundred and sixty patrons in the city and vicinity, twenty-six of whom were outside the city limits, it was held that since the telephone

[52] Gould v. Edison Illuminating Co., 60 N. Y. S. 559, (1899).
[53] Smith v. Capital Gas Co., 132 Cal. 209, (1901).
[54] Fleming v. Montgomery Light Co., 100 Ala. 657, (1892).

company was not doing a general telephone business outside the city limits, it was not compelled to supply instruments to residents beyond the city limits and make connections therewith, and that it was not bound to make uniform charges outside of the city.[55] It seems that such companies have no right to discriminate except when based upon substantial physical differences in the service, as was held in a case where a gas company was supplying gas for both light and heat at the same price, and it adopted a rule fixing a different price for gas furnished for lighting purposes from that furnished for heating purposes. The gas furnished was brought through the same pipes for both purposes and delivered to the consumers at the same point where it went into the pipes put in by the consumer for receiving it, and after passing through a meter was distributed by the consumer through his premises, and used for light or heat or both according to his convenience. Such a difference in price was invalid and unreasonable.[56]

§ 16. Unreasonable Rules. Such companies cannot adopt rules that are oppressive or cause unnecessary inconvenience to its patrons, or that amount to an unjust discrimination. A rule of a gas company requiring its consumers to give free access to their houses and premises at all times by an inspector of the company, for the purpose of examining gas appliances and the removal of meter and service pipes, and providing that the company has the right at any time to cut off the service whenever it deemed it necessary to do so to protect its works against abuse or fraud, was held to be unreasonable. Neither has a water company the right to require a customer to sign a contract which relieves the company from all liability for any scarcity or failure to supply water, or the quality thereof, or to supply water in the event of fire, and expressly exempting it from all liability for failure to supply water for domestic purposes.[57] Neither has such a com-

[55] Crouch v. Arnett, 71 Kan. 49, (1905).

[56] Bailey v. Fayette Gas Fuel Co., 193 Pa. St. 175, (1899).

[57] Dittmar v. New Braunfels, 20 Tex. Civil App. 293, (1899).

pany the power to impose a penalty for violation of any of its regulations, and make submission to such penalty a condition precedent to the right of the customer to service.[58]

§ 17. No Discrimination by Means of Gratuity. A public service corporation cannot discriminate between its customers by conferring a benefit upon some and refusing it as to others, any more than it can directly charge one a higher rate than others. An electric light company, in addition to its business of furnishing lights to a city, engaged in the business of wiring houses and formed a habit of furnishing transformers without extra charge for all houses which were wired for electricity by it, but claimed the right to charge for transformers in cases where it did not do the wiring. A transformer being used to reduce the current from a main line to a lesser current on the line leading into the house for house use, was a necessary appliance to the safe lighting of houses. It was held that the furnishing of this transformer without charge in such cases had the same effect as fixing a lower charge for some of its customers than it charged others, and was, therefore, an unjust discrimination.[59]

The city of Mobile had established a water system for the supply of water to the city and its inhabitants, and also a sewer system and charged the same price for the use of the sewer alone that it did for the sewer and water together. A private corporation was also engaged in furnishing water to the inhabitants of the city in competition with the city, and the private water company brought suit against the city to require it to establish a rate of charge for the sewer alone, alleging that the charge of the same rate for the water and sewer together, as for the sewer alone was, as to the private water company, an unjust discrimination against its customers and the city was required by the court to fix a charge for the use of its sewer alone.[60]

[58] Harbison v. Knoxville Water Co., 53 S. W. Rep. 993, (1899).
[59] Snell v. Clinton Elec. Light, Heat, & Power Co., 196 Ill. 626, (1902).
[60] City of Mobile v. Bienville Water Supply Co., 30 S. Rep. 445, (1901).

§ 18. Telephone and Telegraph Companies. A telephone or telegraph company like all other public service companies, is required to furnish telephone and telegraph facilities without discrimination to all those who will pay for the same and abide the reasonable regulations of the company, but like other public service companies they cannot be compelled to aid in unlawful undertakings. A telegraph company should refuse to send libelous or obscene messages, or those which clearly indicate the furtherance of an illegal act or the perpetration of some crime. They may refuse to have their instruments put in a poolroom which is used for the purpose of betting on horse races, or in a bawdy house, but the right to discriminate against such a business rests in the character of the house or the business for which it is to be used and not in the person, as a keeper of a bawdy house or a gambling house would have a right to have a telephone put in his residence or any other house that he might desire that was not used for such illegal purposes. For like reason a water company could not be required to furnish water, or a light company to supply light, to a house used for carrying on an illegal business.[61]

§ 19. Right to Fix Office Hours. A public service corporation has the right, under its power to make rules, to fix the time when it will keep its office open for the transaction of business. The office hours fixed, like all other rules of such companies to be binding on the public, must be reasonable. In determining the reasonableness of the hours fixed, the ordinary business habits of the community, the nature of the business to be transacted at such office, and population of the community should all be considered in determining whether in a given case the rules of such a company are reasonable. The question of reasonableness or unreasonableness is a question for the courts to decide with reference to the facts of each particular case as it arises. In a case where a telegraph company received a telegram which showed on its face that it required prompt

[61] Godwin v. Caroline Telephone & Tel. Co., 48 S. E. 636, (1904).

delivery, and that it could not be received at the delivering station until after office hours, it was held that by receiving such telegrams the telegraph company assumed the obligation of delivering it, and the company was not permitted to excuse itself for failure to deliver promptly by showing that the telegram was received after business hours at the receiving office.[62] When the hour of presenting a telegram for transmission is an unusual business hour, that fact has been held sufficient to put the sender on inquiry as to whether the telegram would not be delivered, and in the absence of a special contract on the part of the company to receive, transmit, and deliver promptly a telegram received at such an hour, it will be presumed that the sender of the telegram contracting with such company, is bound by the reasonable rules of said company as to business hours.[63]

[62] Brown v. W. U. Tel Co., 6 Utah 219, (1889).
[63] W. U. Tel. Co. v. Neel, 86 Tex. 368, (1894).

CHAPTER II

GENERAL DUTIES AND POWERS OF COMMON CARRIERS

§ 20. Definition. A common carrier is one who undertakes for hire, to transport persons or goods, or both, from place to place, for all persons indifferently. The distinction between a common carrier and a private or special carrier is that the former holds himself out in common, that is, to all persons who choose to employ him, as ready to carry for hire, while the latter agrees in special cases with some private individual to carry for hire.[1] Thus it has been held that a farmer who did hauling was a common carrier, even though transportation was not his principal business.[2] The mode of transportation is immaterial; if there is a general undertaking on the part of any one for hire to transport goods or persons for all who desire such service, such an one is a common carrier.[3] In the aggregate body of common carriers are included the owners of stagecoaches, omnibuses, wagoners, teamsters, cartmen, hackney coachmen, draymen, railroad companies, express companies, fast freight companies, masters and owners of ships, steamboats, barges, canal boats, and public ferrymen, and in general all persons who hold themselves out to the world as ready to carry for all who wish to employ them, for a reasonable compensation.[4]

§ 21. Distinctions between Common Carriers and Other Similar Employments. Towboats are common or special carriers, depending upon conditions of their employment and manner of discharge of their duties. If the towboat is employed as a mere means of locomotion and is under

[1] Allen v. Sackrider, 37 N. Y. 341, (1867).
[2] Gordon v. Hutchinson, 1 W. & S. 285, (1841).
[3] Hall v. Renfro, 3 Met. (Ky.) 51.
[4] 2 Kent's Comm. 598.

entire control of the towed vessel, and the goods in the towed vessel remain in the possession of the owner thereof to the exclusion of the owner of the towboat, or if the towing is casual merely, and not a regular business between fixed points, the towboat is not a common carrier; but if the towboat plies regularly between fixed points, towing for hire, and for all persons, barges laden with goods, and takes into full control and possession the property thus transported, it is under such circumstances a common carrier.[5] Where one had a large circus property including horses, wild animals, and various paraphernalia, which he placed on cars owned by himself for transportation from place to place, and made a written contract with a railroad company to furnish motive power to haul said cars, as a special train to and from certain places fixed in said contract, it was held as to such employment, that the railroad company was not a common carrier, and that the owner of the circus paraphernalia and train could not have demanded as a matter of right that the railroad company furnish motive power to haul the train.[6] It appears that the main distinguishing feature between such employments as the towing of vessels under the direction of the owner of the vessel, and the hauling of the circus train, and that of a common carrier, is that in the two instances mentioned the goods remain in the custody and care of the owner, and such owner directs the motive power; while in the case of a common carrier, the custody and control of the goods is turned over to the carrier, and the carrier directs the operation of the motive power. This is in accord with the ancient grounds for the extraordinary liability of common carriers, which was based upon the carriers' actual custody and control of the goods carried and upon the opportunity thus afforded carriers for cheating and defrauding shippers by combining with thieves in taking the goods under such circumstances that the shipper would be unable to make proof of such collusion and fraud.[7]

[5] Bussey & Co. v. Miss. Valley Trans. Co., 24 La. Ann. 165, (1872).
[6] Coup v. Wabash, St. L. & Pac. Ry. Co., 56 Mich. 111, (1885).
[7] Forward v. Pittard, 1 Term. R. K. B. 27, (1785).

Illustration. A telegraph company is held not to be a common carrier for the following reasons stated by the court:

"A common carrier has exclusive possession and control of the goods to be carried with peculiar opportunities for embezzlement, and collusion with thieves, the identity of the goods received with those delivered cannot be mistaken, their value is capable of easy estimate and may be ascertained by inquiring of the consignor and the carrier's compensation fixed accordingly; and his liability and the damages for failure to carry safely are measured by the value of the goods. A telegraph company is intrusted with nothing but an order or message, which is not to be carried in the form in which it is received, but is to be transmitted or repeated by electricity, which is peculiarly liable to mistake, which cannot be the subject of embezzlement, which is of no intrinsic value; the importance of which cannot be estimated except by the sender nor ordinarily disclosed by him without defeating his own purpose; which may be wholly useless if not forwarded immediately for the transmission of which there must be a simple compensation, and the measure of damages for the failure to transmit or deliver which has no relation to any value which can be put on the message itself." [8]

Express companies are common carriers. The name or style under which a company assumes to carry on its business is wholly immaterial. The real nature of its occupation and of the legal duties and obligations which the law imposes upon it are to be ascertained from the consideration of the kind of service which it holds itself out to the public as ready to render to those who have occasion to employ it. Express companies exercise the employment of receiving, carrying, and delivering goods, wares, and merchandise, for hire, on behalf of all persons who may see fit to require their services. In this capacity they take property from the custody of the owner, assume entire possession and control of it, transport it from place to place, and deliver it at a point of destination to some consignee or agent there authorized to receive it. The fact

[8] Grinnell v. W. U. Tel. Co., 113 Mass. 299, (1873).

that such companies do not own the means by which the carriage is effected does not affect their liability.[9]

§ 22. Liability of Common Carrier. The distinction between the employment of common carrier and that of other related occupations is important because of the extraordinary liability of common carriers. A common carrier by the ancient common law was held liable for all due care and diligence, and for any negligence he was suable on his contract; and further, a common carrier of freight was liable as insurer for its loss by any accident, except such as was caused by the act of God or the king's enemies. It was said by Lord Mansfield that:

"To prevent litigation, collusion, and the necessity of going into circumstances impossible to be unraveled, the law presumes against the carrier unless he shows it was done by the king's enemies or by such an accident as could not happen by the intervention of man, such as storms, lightning, and tempests. If an armed force come to rob the carrier of his goods he is liable for the reason that otherwise the carrier might contrive to be robbed on purpose and share the spoil. No matter what degree of prudence may be exercised by the carrier and his servants, although the delusion by which it is baffled or the force by which it is overcome be inevitable, yet if it be the result of human means, the carrier is responsible." [10]

The term "public enemy" has in general a technical legal meaning. It applies to foreign nations with whom there is open war, and to pirates who are considered at war with all mankind, but it does not include robbers, thieves, rioters, or insurgents, whatever be their violence.[11] And such remains the liability of the common carrier of goods to this day, in the absence of special agreement between the carrier and the shipper.[12]

§ 23. General Duties of Common Carriers. A common carrier is engaged in a public employment, and takes upon

[9] Buckland v. Adams Ex. Co., 97 Mass. 174.

[10] Forward v. Pittard, King's Bench, 1 Term. R. 27, (1785).

[11] So. Ex. Co. v. Womack, 1 Heisk. (Tenn.) 256, (1870).

[12] Cau v. Texas & Pac. Ry. Co., 194 U. S. 427, (1904).

himself public duties, and there are corresponding legal rights upon the part of the public, which are common rights and reasonably equal. A common carrier is bound to carry at reasonable rates such commodities as are in his line of business, for all persons who offer them, as nearly as his means will allow. He cannot refuse to carry a proper article tendered to him at a suitable time and place on the offer of the usual compensation. When he undertakes the business of common carrier he assumes the duties and liabilities of his business as they are defined and laid down by law.

The term "common carrier" implies indifference as to whom he shall serve, and an equal readiness to serve all who apply in the order of their application. A common carrier of freight cannot exercise an unreasonable discrimination in carrying for one and refusing to carry for another, but he may be a common carrier of one kind of property and not of another, but as to the kinds of goods of which he is a common carrier he cannot discriminate unreasonably against any individual in the performance of the public duty he assumed when he engaged in the occupation of common carrier. He may retire from the business and cease to be a common carrier, with or without the public consent, according to the law applicable to his case, but as long as he remains in the service, he must perform the duties pertaining to it. A common carrier of passengers cannot exercise unreasonable discrimination in carrying one and refusing to carry another. It is, however, the duty of a common carrier of passengers to make reasonable discriminating restrictions and refuse to carry those who by reason of their physical or mental condition, would injure, endanger, or annoy other passengers. It is the duty of such carriers to afford reasonable accommodations for its passengers, and this duty is not discharged if they are unreasonably and negligently exposed by the carrier to smallpox or any other transmissible disease. Quiet, moral, and sensitive travelers have cause to complain

of their accommodations if they are unreasonably exposed to the companionship of unrestrained, intoxicated, noisy, profane, and abusive passengers. To allow one passenger to be made uncomfortable by another committing an outrage against the ordinary proprieties of life and common sense, may be as clear a violation of the common right and as actionable a neglect of the common carrier's duty as to permit one to occupy two seats while another stands in the aisle.[13]

§ 24. Carrier's Right to Control Business on Trains. A common carrier is not bound to carry those who wish to engage on their vehicles in the business of selling books, papers, or articles of food, or in the business of receiving and distributing parcels or packages, or to permit the transaction of such business in their vehicles when it interferes with their own interests. If a profit arises from such business, the benefit of it belongs to the carrier, and they are entitled to the exclusive use of their vehicles for such purposes. They can allow the privilege to one and refuse it to another at their pleasure. A carrier may permit an individual to open a restaurant or bar on its conveyances, or to do the business of bootblacking, or of peddling books and papers; such an individual is under its control subject to its regulations, to the end that the business may not interfere with the orderly management of the vehicle. If this were not so, and every one that saw fit could engage in these employments, the control of the vehicle and its good management would soon be at an end. The sale or leasing of these rights to certain individuals and the exclusion of others therefrom are reasonable regulations on the part of the carrier. The right of transportation which belongs to all who desire it, does not include the right to engage in traffic or business, and a carrier has a right to eject one who has become a passenger when that person insists upon exercising his right as a passenger to engage in his own business against the objection of the carrier.[14]

[13] McDuffee v. Portland & Rochester R. R., 52 N. H. 430, (1873).
[14] The D. R. Martin, 11 Blatch. 233, (1873).

§ 25. **Control of Station and Grounds.** Carriers in connection with their railroads usually own or control a terminus provided with offices for the transaction of its business, and waiting rooms, and other facilities for the convenience and protection of the traveling public. While such ownership carries with it the right of control in many respects the same as private property, such terminus to a great extent is a public place. The public have the right to come and go there for the purposes of travel, for taking and leaving passengers and for other matters growing out of the business of the company as a common carrier. But the company has the right to say that no business of any other character shall be carried on within the limits of such property. It has the right to say that no one shall come there to solicit trade simply because it may be convenient for travelers, and to say that none, except those whom it permits, shall solicit for the hack or express business. When notice of such prohibition has been given, the license which otherwise might be implied is at an end, and it is the duty of all persons engaged, or desiring to engage, in any such business to heed the notice and retire from the premises.

§ 26. **Passengers' Rights Preserved.** But in exercising this right of control over its terminal property such a company cannot deprive a passenger of the ordinary rights and privileges of a traveler, among which is the privilege of being transported from the terminus in a reasonably convenient and usual way. The company cannot compel a passenger to take one of certain carriages or none at all, neither can it impose unreasonable restrictions which will amount to that; if a passenger orders a carriage to take him from the terminus such carriage is a private carriage; not in the sense that the passenger has a special property in it so as to be liable for the driver's negligence, but in the sense that it is not standing for hire. Under such circumstances the driver is not engaged in the vocation of soliciting patronage, but is waiting to take one with whom a contract has already been made. Every passen-

ger has the right upon the premises of the carrier to reasonable and usual facilities for arrival and departure. So far as this includes the right to be taken to and from a station or wharf it is immaterial whether he goes in a private or a hired carriage. A hackman who has conveyed passengers to a railroad depot for transportation and is aiding them to alight upon the platform at a station, is as rightfully upon the same as the passengers alighting. Applying the foregoing principles to a case where the owner of a wharf had rules requiring public hacks to obtain licenses from the company and fixing a place for them to stand, and another rule, fixing space for private carriages, providing that no public carriages should be permitted to stand on or adjoining the wharf except its licensees, and a public hackman who had an order from a passenger to meet her backed up on that part of the ground reserved for private hacks and was ordered away, and who thereupon told the superintendent of the wharf that he had an order to meet a passenger, it was held that the hackman could justify his right on the wharf as servant of the passenger and that the superintendent was liable in trespass for ejecting him.[15]

Limitations on Right to Disciminate between Transfer Companies. A common carrier cannot discriminate between transfer men in such a way as to amount to a discrimination between its passengers or prospective passengers, or that will put an unreasonable burden on some of them, in traveling to and from its trains. In a case where one transfer company was given by a railroad company the exclusive right to occupy a part of the railroad platform and all other transfer companies were excluded therefrom, and the effect was to put the privileged transfer company about fifty feet closer to where passengers were discharged from trains than the other transfer companies, such an arrangement was held to be an unjust discrimination, because it had the effect of compelling passengers to employ the privileged company at whatever price it might see fit

[15] Griswold v. Webb, 16 R. I. 649, 19 Atlantic 143, (1889).

to charge, or submit to the inconvenience of going farther away to obtain such service.[16]

§ 27. Proper Discrimination Relative to Transfer Companies. Any rule of a common carrier granting exclusive privileges to favored transfer companies, that results in furnishing added or more convenient facilities to the public for the transaction of business with such carrier, will be upheld by the courts. In a case where a railroad company permitted a cab company to enter its passenger trains and solicit the carriage of baggage from its passengers before reaching a city, and allowed the cab company's agents access to the passenger station for the purpose of soliciting patronage, and allowed the company the privilege of using the office of the baggage room of the depot, and gave it the privilege of checking the baggage of prospective passengers at hotels and at their residences in advance of delivery of the baggage at the passenger station, and all of which privileges were denied to all other transfer men of the city; it was held that the railroad company was not bound to furnish facilities such as were provided for in the above arrangement, but such privileges afforded to passengers and customers of the company promoted the convenience of the traveling public and that the railroad company had no right to discriminate between passengers, either in the receipt or delivery of baggage or in the manner in which they were received or discharged, but this rule of impartiality applied to railroads in their duty to passengers, and did not prohibit their right to control the use of their own property by granting rights to one not required to be furnished by railroad companies, and excluding others engaged in such business and desiring to transact business thereon.[17]

Right to Refuse Solicitor as Passenger. A common carrier may refuse to receive as a passenger one who intends to take advantage of his position as passenger to solicit from other passengers. Where *A* was the agent of a line

[16] Mont. Union Ry. v. Langlois, 9 Mont. 419, 24 Pac. 209, (1890).
[17] Kates v. Atlanta Baggage & Cab Co., 107 Ga. 636, (1899).

of stagecoaches and his object was to take passage on a steamboat and while on the boat as such passenger, to solicit other passengers for business for such stagecoach line, the proprietors of the steamboat having given notice that they would not permit agents of that line to solicit passengers on their boats, refused to receive such agent as a passenger, and it was held that said proprietors were justified in such refusal, the court saying:

"That the right of passengers to a passage on board of a steamboat was not an unlimited right, but that it was subject to such reasonable regulations as the proprietors may prescribe for the due accommodation of passengers and the management of their business."

Not Bound to Serve Those Refusing to Abide by Reasonable Regulations. Such proprietors have the further right to consult and provide for their own interests in the management of such boats as incident to their right of property therein. They are not bound to admit passengers on board who refuse to obey the reasonable regulations of the boat. Nor are they bound to admit passengers whose object it is to interfere with the interests or patronage of the proprietors, so as to make the business less lucrative to them. While steamboat proprietors, holding themselves out as common carriers, are bound to receive passengers under ordinary circumstances, they may refuse to receive them if there be a reasonable objection. Passengers are bound to obey the orders and regulations of the proprietors, unless they are oppressive and grossly unreasonable. Whoever goes on board under ordinary circumstances impliedly contracts to obey such regulations, and may be justly refused passage if he willfully resists or violates them. If a person who has habitually theretofore violated the rules of the company applies for passage, the proprietors have a right to presume that he is asking passage with a like intent. If a person were to come on board who had theretofore habitually been drunk or gross in his behavior, or obscene in his language, the proprietors may refuse to

allow him passage upon the presumption that his conduct would again be objectionable.[18]

§ 28. Right to Classify Passengers. Common carriers have the undoubted right to make reasonable rules and regulations for the safety and comfort of passengers traveling on their lines of road. A railroad cannot capriciously distinguish between passengers on account of their nativity, color, race, social position, or their political, or religious beliefs. Whatever discriminations are made must be on some principle, or for some reason that the law recognizes as just and equitable and founded in good public policy. A railroad company can, by rule, require those of its passengers who desire to smoke to occupy an apartment or car set aside by it for the use of such persons, and may exclude them from other cars where smoking is prohibited. It may maintain separate cars for ladies unaccompanied and those accompanied by escorts, but it has been held that a colored woman could not be denied the privilege of occupying the ladies' car and be made to occupy a seat in a car mostly occupied by men. However, it has been held not to be an unreasonable regulation to seat persons so as to preserve order and decorum and prevent trouble arising from well-known repugnances, and that a rule that required a colored woman to occupy a separate seat in a car furnished by the company equally as comfortable and safe as that furnished for other female passengers was not an unreasonable rule.[19]

§ 29. Right to Refuse Passengers. If there are reasonable objections to a proposed passenger a carrier is not required to take him, as where one applied for passage to San Francisco who had been theretofore banished by a vigilance committee, it was held proper to refuse a passage if, in the opinion of the master of the boat, his return to San Francisco would promote further difficulty there; but after having admitted him as a passenger and received his fare, unless he misbehaves during the journey they cannot

[18] Jenks v. Coleman, 2 Sumn. 221, (1835).
[19] C. & N. W. R. R. Co. v. Williams, 55 Ill. 185, (1870).

expel him.[20] It has been held that a carrier may refuse to carry one traveling to a place for the purpose of engaging in rebellion against the United States government.[21]

Persons Physically or Mentally Deficient. A regulation of a railroad company that no blind person whatever shall travel thereon unaccompanied by an assistant, no matter how skillful or expert a traveler he may be, and no matter how well qualified he may be in every respect to travel on cars unaccompanied, is not a reasonable rule, and an unconditional rule that an insane person shall not be carried is also unreasonable, but the company would have power to require that an insane person be accompanied by an attendant, and that a blind person under such disability therefrom that he could not travel alone should be accompanied by an attendant.[22]

Because of Reputed Bad Character. A common carrier has in general no right to refuse to carry a passenger because of his bad character, either actual or reputed. In a case where a railroad company refused to receive a colored woman as a passenger alleging that she was a notorious and public courtesan, addicted to the use of profane language and offensive habits of conduct in public places, it was held as follows:

"The same principles of law were to be applied to a woman as to a man in determining whether exclusion was unlawful or not; that unchaste women had a right to travel on the streets or on the public highways, and other people who traveled must expect to meet them in such places, and as long as their conduct was not objectionable in such places they could not be excluded."

A common carrier is bound to carry good, bad, and indifferent, and has nothing to do with the morals of its passengers if their behavior be proper while traveling. Neither can the carrier use the character for chastity of his female

[20] Pearson v. Duane, 4 Wall. 605, (1867).

[21] Turner v. N. C. R. R. Co., 63 N. C. 522, (1869).

[22] Zachery v. Mobile & Ohio R. R. Co., 75 Miss. 746, (1898); Owens v. Macon & Brunswick R. R. Co., 119 Ga. 230, (1903).

passengers as a basis for classification, so that he may put all chaste women, or women who have the reputation of being chaste into one car, and those known or reputed not to be so in another car. Such a rule would put every woman purchasing a railroad ticket on trial for her virtue before the conductor as her judge. It would destroy the peace of mind of all sensible and sensitive women in traveling, no matter how virtuous. They would be in constant fear lest they might be put into or unconsciously occupy the wrong car or the wrong seat. The police power of the carrier is sufficient protection to other passengers, and he can remove all persons, men or women, whose conduct at the time is annoying. He can no more classify women according to their reputation for chastity than he can so grade the men.[23] A common carrier as an incident to its business, not only has power but is bound to take all reasonable and proper means to insure the safety, and provide for the comfort and conveniences of passengers. It follows that it is its duty to repress and prohibit all disorderly conduct in its vehicles, and to expel or exclude therefrom any person whose conduct or condition is such as to render acts of impropriety, rudeness, indecency or disturbance either inevitable or probable.[24]

§ 30. Rules of Carrier. A common carrier like other public service corporations has the power to make rules binding alike upon itself and its patrons for the management of its business. It has been held that a rule prohibiting passengers from sitting or standing on the rear platform of a street car is valid and reasonable, and that where a passenger paid his fare and claimed the right to stand on the platform of the car in violation of such rule, offering as a reason that he had a sick headache and to go inside of the car would make him sick, was properly ejected for his refusal to obey the rules.[25] Where one entered a street car carrying a goat and paid his fare and procured a transfer,

[23] Brown v. Memphis C. R. R., 5 Fed. Rep. 499, (1880).
[24] Vinton v. Middlesex R. R. Co., 11 Allen 304.
[25] Montgomery v. Buffalo Ry. Co., 165 N. Y. 139, (1900).

and was later ejected, it was held to be proper on the part of the company to make regulations with respect to carrying of animals on its cars.[26]

Tickets at Station Gates. A railroad company may make and enforce rules requiring persons passing through the gates of its passenger station, for the purpose of taking trains, to exhibit their tickets to the gatekeeper, and have them punched by him, and also providing that no passenger shall be allowed to pass out of any gate after the train indicated by his ticket has started, or to board any train while in motion. All persons having notice of such rule, and reasonable opportunity to comply with it are bound to observe it in order to obtain the right to pass through the gates or to take a train in the railroad depot, and a railroad company may use such force as may be reasonably necessary to prevent the violation of such rules. Where a passenger went through the gates at the depot of a company having such regulations, was called back and made to exhibit his ticket, and was thereby caused to miss his train, he was held not entitled to a judgment for damages.[27]

Conductor's Right to Ticket. A railroad company has a right to require the surrender of a ticket, or the payment of a fare from every passenger, and the fact that one actually purchased a ticket, and that fact was known to the agent who sold it, and to the gatekeeper who examined it, and to employes on the train who saw it, will not release the passenger from the obligation to surrender it to the conductor, or pay his fare. The conductor cannot be required to hear evidence or investigate the good faith of the passenger's excuses for non-delivery of a ticket, nor to wait until he arrives at the next station and, by telegraphic correspondence with the selling agent, undertake to verify the correctness of a passenger's statement that he purchased a ticket, or to determine the character and validity of the ticket sold. It is manifest that such a course would necessarily give rise to delay and seriously interfere with

[26] Daniel v. N. J. St. Ry. Co., 64 N. J. Law 603, (1900).
[27] Dickerman v. St. Paul Depot Co., 44 Minn. 433, (1890).

the operation of trains and the rights of the traveling public.[28] But if the passenger is unable to produce a proper ticket because of the negligence or mistake of the servants or agents of the railroad company, the company will be liable if the passenger is ejected. In a case where a round trip ticket was purchased by a passenger, and by mistake of the conductor on the going trip, the return coupon was cancelled, and the error was afterwards marked on the ticket by the conductor, but not in the way required by the rules of the company under such circumstances, and the passenger was assured by such conductor that the marks he had put on the return coupon would make it all right, and the passenger on the return trip presented the ticket to another conductor and it was refused, and he was ejected, it was held that the company was liable for ejecting him.[29] The conductor of a street railway car cannot reasonably be required to take the mere word of a passenger that he is entitled to be carried by reason of having paid a fare to the conductor of another car, or even to receive and decide upon the verbal statements of others as to the fact. The conductor has other duties to perform, and it would often be impossible for him to ascertain and decide upon the right of the passenger except in the usual way by means of checks or tickets. It is no great hardship upon the passenger to put upon him the duty of seeing to it, in the first instance, that he receives and presents to the conductor the proper ticket or check, or if he fails to do this to leave him to his remedy against the company for a breach of its contract. Otherwise the conductor must investigate and determine the question as best he can while the car is on its passage. A railroad company is not required to give credit for the payment of a single fare, and if the conductor was required to determine upon the truth and justice of a passenger's claim to be carried otherwise than by the production by the passenger of a proper ticket or the payment of the cash fare, a wrong decision against the passenger would

[28] Hart v. So. Ry. Co., 119 Ga. 927, (1904).
[29] Phila. Wilm. & Balt. R. R. Co. v. Rice, 64 Md. 63, (1885).

submit the company to liability in an action at law.[30] A passenger purchases his ticket subject to the reasonable regulations of the railroad company, and it is an implied condition in his contract that he will submit to such regulations, and if he willfully refuses to be bound by them he repudiates his contract, and after such repudiation he cannot claim the right to ride on his ticket, which is the evidence of his contract with the railroad company. In a case where a passenger refused to show his ticket on the demand of the conductor, and refused to leave the cars on request, and was put out, and then produced and offered to surrender his ticket, it was held that he had then forfeited his right to be carried on the train, and that the conductor properly refused to permit him to re-enter the train.[31]

Additional Charge When Fare Paid on Train. Railroad companies in pursuance of their power to make reasonable regulations, may fix not only the amount of fares, but the time, place, and mode of payment, and may charge an additional or higher rate of fare to those who do not purchase tickets before they enter the cars. In a case where a passenger failed to reach the depot in time to purchase a ticket, and the statutes of the State provided that no charge should exceed three cents per mile for through passengers and three and one-half cents per mile for way passengers, the passenger boarded the car and when the conductor called upon him for his ticket he stated that he had none and tendered to the conductor fourteen cents in cash, that being at the rate of three cents per mile. The railroad company had a regulation requiring passengers without tickets to pay the conductor in addition to the regular three cents per mile the additional sum of ten cents. The amount of excess to be paid in excess of the regular fare was uniform, and upon its payment the conductor was required to issue a check to the passenger which was redeemable at ten cents on presentation at any ticket office of the company along its line. Notice of this regulation had

[30] Bradshaw v. So. Boston Ry. Co., 135 Mass. 407, (1883).
[31] State v. Campbell, 32 N. J. Law 309, (1867).

been given to the public by printed cards posted at the company's ticket offices. It was held that the regulation was reasonable and that a passenger could be ejected from the train for refusal to pay the excess fare.[32] But such a regulation is invalid and cannot be sustained unless the railroad company affords reasonable opportunities and facilities to passengers to procure tickets, and thereby to avoid the disadvantage of paying the higher rate. When such a regulation is established, and a passenger endeavors to buy a ticket before he enters the cars, and is unable to do so on account of the fault of the corporation or its agents, and he offers to pay the ticket rate on the train and refuses to pay the car rate, it is unlawful for the corporation, or its agents, or servants to eject him from the train. He is entitled to travel at the lower rate, and the corporation is a trespasser, and liable for the consequences if he is ejected from the train by its agents or servants. The passenger may under such circumstances, either pay the excess demanded under protest, and afterwards recover it by suit, or he may refuse to pay it and hold the corporation responsible for damages in case he is ejected from the train.

In a case where a prospective passenger was prevented from purchasing a ticket by the failure of the ticket agent to open the office long enough before train time to enable him to purchase a ticket, it was held that he was entitled to recover actual damages, but that he could not recover exemplary damages, unless the expulsion was characterized by malice, recklessness, rudeness, or willful wrong on the part of the agents or servants of the corporation.[33]

Limited Time for Use of Ticket. A passenger has a right to be conveyed in the cars of a railroad company without making any special contract for transportation. Upon payment of the usual fare the company is bound to convey him, and is under all the obligations imposed by law on common carriers, so far as they relate to the trans-

[32] Rees v. Penn. R. R., 131 Pa. 422, (1890).
[33] Forsee v. Ala. Great So. Ry., 63 Miss. 66, (1885).

portation of him as a passenger. It is competent to vary these obligations by special agreement on valuable consideration between the passenger and the company. But if the passenger chooses to do so, he may stand on his legal rights, and elect to be carried to his destination without making any special contract. But before the extraordinary liability of a railroad company can be varied, there must be a consent of the passenger founded on valuable consideration. The ticket, ordinarily, is only a token showing that the passenger has paid his fare, but where the ticket is sold for less than the usual rates on the condition that it shall not be used after a limited time, if the passenger accepts and uses the ticket, he makes a contract with the company according to the terms stated, and the reduction in the fare is a consideration for his contract. It is true he pays his fare before he receives the ticket, but if he has been misled or misinformed by the seller of the ticket as to its terms, he has a right to return the ticket and receive back his money. In a case where a passenger purchased an excursion ticket, the return coupon of which provided that it must be used "within three days, including the day of sale", and used the going coupon of the ticket, and after the expiration of the three days boarded a train for return, and the conductor refused to receive the ticket, the passenger claiming that the selling agent told him the ticket was good until used, and the passenger was ejected by the conductor at the next regular station of the train, and after he was ejected offered to pay the regular cash fare from that station to the point of his destination and that was refused, the court held that he was properly ejected, and the conductor's refusal to accept payment for the remainder of the return trip was also proper for the reason that if the conductor had received the payment of the fare for the remainder of the trip, the passenger would have been carried the whole return trip for less than the regular fare.[34] A railroad company has power to fix a reasonable limit of time within which a ticket shall be used, and it is

[34] Penington v. Phila. Wilm., & Balt. R. R. Co., 62 Md. 95, (1883).

generally sufficient if the trip is begun within the time fixed.[35]

§ 31. Time of Trains. Railroad companies in their own interests and also in discharge of their duty to the public, are required to fix and promulgate time tables showing the time of arrival and departure of trains from its stations, and the advertised time of the arrival and departure of trains enters into the contract which a passenger makes with the company when he purchases his ticket, but such advertised time of the running of trains may be changed from time to time as the interests of the railroad company and the convenience of the traveling public may require. Railroad companies often find it necessary to vary time of running their trains, and they have the right under reasonable limitations to make this variation even as against those who have purchased their tickets, but if the time of the train is changed, a person who presents himself at the advertised hour and demands a passage is not bound by the change unless he has had reasonable notice of it, and may recover damages for the failure of the railroad company to relieve itself from this obligation to run its train as advertised; it must publish notice of the change as extensively as it published its regular time table, and if the same publicity is given of a change in the time of trains as was given of the former time table, the public will be bound by it. In a case where a train was regularly advertised and run leaving Station A at 9:30 P. M., but to enable a certain number of its passengers to attend an entertainment the leaving time of the train was postponed to 11:15 P. M., and notice of the postponement of the time of leaving of said train was given by printed hand bills posted up in the cars and stations a day or two before the day on which the train was to be so delayed, but notice was not given in the newspapers where the regular time table was published, it was held that the railroad company was liable to a passenger who had purchased his ticket and presented himself for passage at the regular train time,

[35] Elliott on Railroads, § 1598.

and who had no knowledge of the change in the leaving time of the train.[36]

§ 32. Time Stations Kept Open. A railroad company may by rule fix the time when it will open and close its station and waiting rooms, and these rules, when reasonable, may be enforced as against the traveling public. The reasonableness of such rules will depend on the circumstances of each particular case. In determining the reasonableness of such rules the number of trains, and the hours at which they arrive and depart, and the population of the community where the station is situated, and opportunity of prospective passengers to obtain shelter at other places, should all be taken into consideration. Where a prospective passenger entered the waiting room of a railroad company's depot at eight o'clock at night with the intention of remaining there until the departure of the next train, which would leave at 1:20 the next morning, it was held that he had no right to remain in the depot for that length of time. The rules fixing times for opening and closing of depots must be enforced by the servants or agents of the company with reference to circumstances, and such rules should be varied in cases where trains are delayed, or where there is an unusual amount of traffic, or any other happening out of the ordinary that makes it convenient and reasonably necessary for the public to use the depot outside of the ordinary hours. In the management of its depot a railway company may exclude from their waiting rooms all persons other than passengers, their agents, servants, and escorts, and people having business of some kind with the company.[37]

§ 33. Proper Tender of Fare. A street railway under its power to make rules for the regulation of its business, has the right to fix the maximum amount of change its conductors shall be required to furnish to a passenger in making change for a bill, or coin tendered in payment of a fare. The amount fixed must be reasonable, taking into

[36] Sears v. Eastern R. R., 14 Allen 433, (1867).
[37] Phillips v. So. Ry., 124 N. C. 123, (1899).

consideration the size of the coins and bills in common circulation in the city where the street railway is being operated, and also its population, and the relative opportunity of the street car company's conductors and its customers to obtain small change. It is evident that it would be unreasonable in most cases to require the passenger to tender the exact fare. Neither can the street railway company be required to furnish change for any amount however large. It is not necessary that prospective passengers shall have notice of the adoption of such reasonable rules by the company in order that the public may be bound by them. It has been held by the Supreme Court of California that the tender of a five dollar gold piece in payment of a five cent car fare was not unreasonable, and in the course of opinion the court said:

"The true rule must be, not that the passenger must tender the exact fare, but that he must tender a reasonable sum, and that the carrier must accept such tender, and must furnish change to a reasonable amount."

The obligation to furnish a reasonable amount must be considered as one which the law imposes from the nature of the business.[38] The Court of Appeals of the State of New York held, that the rule of a street railway company fixing two dollars as a proper tender to its conductors in payment of a five cent fare was reasonable, and that such a conductor had the right to refuse to accept five dollars in payment of such a fare. In the course of its opinion the court said:

"In a large city like New York, the round trip of a car on any street car line means a very considerable number of fares paid in, and the necessity for the conductor to carry and pay out a large amount of small change. When the defendant (the street car company) enacted the rule requiring its conductors to furnish change to a passenger to the amount of two dollars, it did all that could reasonably be expected of it, in consulting the convenience of the

[38] Barrett v. Market St. Ry., 81 Cal. 296, (1889); Funderberg v. Augusta & Aiken Ry. Co., 61 S. E. 1075, (1908).

general public, and it would be unreasonable and burdensome to extend the amount to five dollars. It would require conductors to carry a large amount of bills and small change on their persons, and greatly impede the rapid collection of fares." [39]

In a case where a twenty dollar gold coin was tendered to a conductor on a railroad train, in payment of a fare amounting to one dollar and thirty-five cents, it was held to be too large, and the court said:

"If any or all of the passengers might put the conductor to the trouble of giving back so much change as would have been required in this case, it would be impossible that the business could be transacted with the expedition which is necessary or with proper caution, for there would be people who would soon take their chances at putting off counterfeit coins or bills, if they found that the conductor was obliged to receive them under circumstances which did not admit of his taking time to scrutinize them, and a person rushing into a car without a ticket has no reason to expect he will find the conductor prepared to change a twenty dollar gold piece, for the simple reason that the conductor relies upon receiving tickets from the passengers, or if money is paid to him instead, that it will be paid with reasonable regard to what is convenient under the circumstances." [40]

In the case of railroads the conductors have a right to expect passengers to board its trains with tickets, purchased as required by the rules of such companies, and they will not be required to furnish change in large amounts to passengers desiring to pay their fare on the train.

§ 34. Express Cases. At common law there was no duty resting upon a common carrier to carry express companies without discrimination, and such companies had a right to do the express business of whatever express company they saw fit, and to make such special contracts upon such terms and conditions as should be agreed upon between the carrier and the express company, and other express

[39] Parker v. Cent. Park N. & E. R. R. Co., 151 N. Y. 237.
[40] Fulton v. Grand Trunk R. R. Co., 17 U. C. Q. B. 428.

companies could not complain if a carrier did the carrying for one company, and entirely refused to do it for such others. In the express cases it was shown that no railroad in the United States had ever held itself out as a common carrier of express companies, but on the contrary, that no railroad company had ever taken an express company on its trains for business except under a special contract, in which the respective rights and duties of the railroad company and of the express company were carefully fixed and defined therein, and with very few exceptions only one express company had been allowed to do business on its road at the same time. It having been thus shown that, based on custom, there was no common right on the part of express companies to be carried by the railroads, in showing that from the nature of the business of express companies there was no duty resting on railroad companies to carry them arising out of the general obligation to serve the public, the Supreme Court of the United States said:

"The reason is obvious why special contracts in reference to this business are necessary. The transportation required is of a kind which must, if possible, be had for the most part on passenger trains. It requires not only speed, but reasonable certainty as to the quantity that will be carried at any one time. As the things carried are to be kept in the personal custody of a messenger or other employe of the express company it is important that a certain amount of car space should be specially set apart for the business, and that this should as far as practicable, be put in the exclusive possession of the expressman in charge. As the business to be done is 'express', it implies access to the train for loading at the latest, and unloading at the earliest convenient moment. All this is entirely inconsistent with the idea of an express business on passenger trains free to all express carriers. Railroad companies are by law carriers of both persons and property. Passenger trains have from the beginning been provided for the transportation, primarily of passengers and their baggage. This must be done with reasonable promptness and reasonable comfort to the passengers. The express business on passenger trains is in a degree subordinate to the passenger business, and it is consequently the duty

of a railroad company in arranging for the express, to see that there is as little interference as possible with the wants of passengers. This implies a special understanding and agreement as to the amount of car space that will be afforded and the conditions on which it is to be occupied, the particular trains that can be used, the places at which they shall stop, the price to be paid, and all the varying details of a business which is to be adjusted between two public servants, so that each can perform in the best manner its own particular duties. All this must necessarily be a matter of bargain, and it by no means follows that because a railroad company can serve one express company in one way, it can as well serve another company in the same way, and still perform its other obligations to the public in a satisfactory manner. The car space that can be given to the express business on a passenger train is, to a certain extent, limited, and as has been seen that which is allotted to a particular carrier must be, in a measure, under his exclusive control. No express company can do a successful business unless it is at all times reasonably sure of the means it requires for transportation. On important lines one company will at times fill all the space the railroad company can well allow for the business. If this space had to be divided among several companies, there might be occasions where the public would be put to inconvenience by delays which could otherwise be avoided. So long as the public are served to their reasonable satisfaction, it is a matter of no importance who serves them. The railroad company performs its whole duty to the public at large, and to each individual when it affords the public all reasonable express accommodations. The railroad company owes no duty to the public as to the particular agencies it shall select for that purpose, provided they are always such as to insure reasonable promptness and security, seems to imply that a railroad at the present time is required, in the proper discharge of its public duties, to furnish some sort of facilities for the transaction of business of the kind usually carried on by express companies."[41]

§ 35. Not Bound to Carry for Other Common Carriers. The public duties of a common carrier do not include the duty to carry the goods of a rival carrier. In a case where *A* was engaged in gathering together small packages from

[41] The Express Cases, 117 U. S. 1, (1886).

shippers, and charging smaller rates than an express company that was operating in that community charged for packages of that size, and after packing them into one hundred pound packages, demanded that said express company carry them at its one hundred pound rate, which was lower than the rate for smaller packages, it was held that under such circumstances the express company could not be required to carry the one hundred pound packages at the lower rate,[42] as the rate was unreasonable under the circumstances and that the express company was not a common carrier for a rival express company, and that it could not be required to carry goods for a rival to its own destruction.

In general, a public service corporation can not be required to render service to a competitor or do anything that will enable one to get business away from it for the benefit of a competitor,[43] as an innkeeper is not bound to entertain an agent for a rival inn who is seeking to obtain his customers for such rival inn.

§ 36. Railroads Common Carriers of All Kinds of Goods. At common law any person could be a common carrier of all kinds, or any kind, or just such kinds of personal property as he chose, no more and no less. The common law as to common carriers had become fairly well settled and fixed before railroads came into existence, but when railroads came into use the same rules were applied to them as had been applied to other carriers. From this it seems that railroads might be created for the purpose of carrying one kind of property only, or for carrying many kinds, or all kinds which can be carried by railroads. However, it will be presumed that they were created for the purpose of carrying all kinds of personal property. It is not reasonable to suppose that they are created simply for the purpose of being carriers of such articles only as were carried by common carriers under the early common law, for if such were the case they would be carriers of but very few

[42] Johnson v. Dominion Ex. Co., 208 Ontario 203, (1896).

[43] Jencks v. Coleman, 2 Sumn. 221, (1835), Fed. Cas. No. 7258.

of the innumerable articles that are now actually carried by railroad companies. It can hardly be supposed that they were created for the mere purpose of taking the place of pack horses, wagons often drawn by oxen, or the other primitive means of transportation that were used in the early days in England. Railroads are accustomed to carry all kinds of property, and whenever a railroad company undertakes the carriage of any article over its road, the railroad will be presumed to be a common carrier of such articles.[44]

The fact that a railroad company begins to run a train for the accommodation of a particular business, in pursuance of a special contract with the owner of such business, will not make it as to such train, a special carrier, and enable it thereby to discriminate against another engaged in the same kind of business; as where a railroad company by an agreement with a certain newspaper publishing company, whereby the newspaper company guaranteed a certain revenue from the running of such train, agreed to run a special early morning train, carrying only the newspapers of such publishing company, and another newspaper company demanded that the railroad company receive and transmit its packages of newspapers to its several agents, at various stations along the line where the train was scheduled to stop, and the railroad company refused to transport said newspapers on the ground that it was a private carrier of newspapers, but conceded that the same train was a common carrier of passengers, and other baggage, and all mail and express. It was held that a common carrier might become a private carrier for hire when, as a matter of accommodation or special agreement, he undertakes to carry something which it is not his business to carry; e. g., if a carrier of country produce running a truck boat should be requested to carry a keg of silver or a load of furniture, he might refuse to receive such freight, or he might make such special agreement for its carriage as he might choose to make, but when a carrier has a regular

[44] Kans. Pac. Ry. Co. v. Nichols, Kennedy & Co., 9 Kans. 235, (1872).

established business for carrying all or certain kinds of articles, it is a common carrier, and a special contract about its responsibility in a given case does not divest it of that character; and that the duty of said railroad as a common carrier was, that it should deal fairly and impartially with all who seek as passengers or shippers of freight to avail themselves of its service, and that said railroad was impressed with a duty to the public, that could only be discharged by extending to each member constituting the public equal service, and that the refusal to receive and transmit the packages of newspapers from the other publisher was a violation of its public duties, and that its contract made with the first publisher not to receive such packages was void.[45]

§ 37. Usual Demands for Facilities. A common carrier of goods is required to provide sufficient facilities to receive and carry all goods and passengers that are offered at its stations on payment or tender of the usual freight rate; and it has no right to discriminate in favor of one shipper over another, either in rates or facilities. When the carrier has furnished itself with the appliances reasonably necessary and adequate to transport the amount of freight which may, in the usual course of events, be reasonably expected to be offered for carriage, it has done its whole duty in that regard. The sufficiency of such accommodations must be determined by the amount of freight and the number of passengers ordinarily transported on any given line of a road. The duty of a company to the public in this respect is not peculiar to any season of the year, or to any particular emergency that may arise in the course of its business. The amount of business ordinarily done by the road is the only proper measure of its obligation to furnish transportation. If, by reason of a sudden and unusual demand for stock or produce in the market or from any other cause there should be an unexpected influx of business to the road, its obligation will be fully discharged by shipping such stock or produce in the order

[45] News Pub. Co. v. So. Ry. Co., 110 Tenn. 684, (1903).

and priority of time in which it is offered to the road for shipment.[46]

§ 38. **Order of Rendering Service.** Where a public service corporation is not able upon demand to accommodate all who apply for its services, it is the duty of such a company to render such service in the order in which applications are made at the place where the service is to be rendered, or in the case of common carriers where the carriage is to begin. In a case where one applied for accommodations in a sleeping car and was informed that the berths were then all sold for a certain part of the distance for which the applicant desired accommodations, it was held that the conductor had a right to refuse to sell the berth until the train arrived at the station where one of the berths would be vacated, and that if there were other applications for accommodations at such station, the conductor had a right to sell to the one first making application at that place.[47] But the rule that service is to be rendered and accommodations furnished in the order in which it is applied for, applies to railroads only when the service demanded is of the same class. It is the duty of a common carrier to forward trains carrying passengers in preference to trains transporting freight. In a case where trains were delayed on account of deep snow, it was held that the owner of cattle in transportation could not complain that the extraordinary efforts which were made by the railroad to forward passengers were not made to forward his cattle.[48]

Where two kinds of property, one perishable and the other not, are delivered to the carrier at the same time by different parties for transportation, and the carrier is unable to carry all the property presented for transportation, it is the duty of the carrier to transport the perishable property first.[49]

§ 39. **Effort to Render Service.** A public service corpo-

[46] State *ex rel.* Crandall v. C. B. & Q. R. R. Co., 72 Neb. 542, (1904).
[47] Searles v. Mann Boudoir Car Co., 45 Fed. Rep. 330, (1891).
[48] Breddon v. Great Northern Ry. Co., 28 L. J. Exch. (N. S.) 51, (1858).
[49] Tierney v. N. Y. Cent. & Hud. R. R. R., 76 N. Y. 305, (1879).

ration is bound to render service only in the usual and customary method under which its operations are conducted, and it is ordinarily not bound to make extraordinary efforts and expend large sums of money in an effort to render a small service, as in a case where a telephone company in good faith fixed the limits within which it was to conduct its business, and in accordance with the usual and approved methods of well-managed companies divided its area into districts, to be served by wires in cables to a point within each of said districts, convenient for its distribution. There is no discrimination at common law, unless an applicant within a particular district is discriminated against and others served within the same general area, in like situation and under like circumstances with himself. And such a company would not be required to put in a special wire to serve a single subscriber in a district served by one of its cables in which all the wires in the cable were in use.[50]

§ 40. Duty to Apportion and Distribute Equipment. A railroad company must distribute its means of transportation at the various stations for receiving passengers and freight along the entire line of its road, so as to afford a reasonable amount of accommodation to all. No one station should be furnished with means of transportation to the prejudice of another, but a distribution should be made among all in something like a just proportion to the amount of business ordinarily done at each. It is the duty of a railroad company to receive all freight that may be offered, and within a reasonable time, and in the order in which it is offered, to transport the same to any other point on the line of its road that may be designated by the owner or other person having charge of it. This duty to the public must be performed in good faith, and without partiality or favor to any one. Every individual in the community, by complying with the prescribed rules and regulations of the company, has an equal right to demand the performance of this duty, and the law does not excuse a discrimi-

[50] Cumberland Telephone & Tel. Co. v. Kelly, 160 Fed. Rep. 316, (1908).

nation in favor of any particular station on the line of its road.[51]

§ 41. Notice by Shipper. A prospective shipper must give reasonable notice of the kind and quantity of freight he desires to ship, and of the time he desires to make such shipment. A shipper has no right to expect or require the railroad company to have equipment at all times ready and waiting to serve his purposes. Such notice to be reasonable must be sufficient to enable the company by the exercise of reasonable diligence, to furnish the desired equipment without interfering with previous orders from other shippers at the same station, or jeopardizing its business on other portions of the road. The company owes the same duty to shippers at any other station of the same business importance. The rights of all shippers applying for such cars under the same circumstances are necessarily equal. No one station, much less any one shipper, has the right to command the entire resources of the company to the exclusion or prejudice of other stations and other shippers. It is the duty of the carrier to inform the shipper within a reasonable time after such notice, whether it is able to furnish such equipment at the time and place designated by the shipper.[52]

§ 42. Furnish Reasonable Protection of Goods. It is the duty of a common carrier who receives goods for transportation to furnish equipment reasonably adapted for the preservation of such goods during the time required for their transition from the place of shipment to the place of destination, and if the goods are of such a nature as to require for their protection some other kind of car than that required for ordinary goods, and cars adapted for such goods are in customary use by carriers, it is the duty of the carrier to provide such cars for their carriage. A railroad company cannot escape responsibility for its failure to provide cars reasonably fit for the conveyance of the particular class of goods it undertakes to carry, by offer-

[51] Ballentine v. N. Mo. R. R. Co., 40 Mo. 591, (1886).

[52] Ayres v. C. & N. W. R. R. Co., 71 Wis. 372, 37 N. W. 432, (1888).

ing the excuse that such equipment is owned by another company, or that it was the duty of the other company under a contract with the railroad company accepting such goods to furnish ice, or any other protection that might be necessary for the protection of the goods.[53]

§ 43. Must Handle Cars of Other Companies. It is the duty of a railroad company to afford reasonably adequate means to effect the prompt transportation of freight, and to that end is required to transfer freight in cars belonging to other roads when reasonably necessary to effect prompt and safe shipment; as was said by Judge Cooley:

"A railroad company is compelled *first,* to receive and transport over its road all the varieties of freight cars which are offered to it for the purpose and which are upon wheels adapted to its gauge. Because the necessities of commerce demand it, it can not and would not be tolerated that cars loaded at New York for San Francisco, or at Boston for Chicago, should have their freight transferred from one car to another whenever they passed upon another road. Time would be lost, expense increased, injuries to freight made more numerous, and no corresponding advantage accrue to any one. It is compelled to do so, *second,* by its own interest. To attempt to stop every car offered to it at its own termini, that the freight might be transferred to its own vehicles, would be to drive away from its line a large portion of its traffic, and compel it to rely upon a local business for which it must increase its charges to make up if possible for what it would lose." [54]

§ 44. Right to Make Rules as to Shippers. A railroad company has the right to make reasonable regulations, applicable to all shippers, as to the manner in which a commodity shall be received for transportation, and has the power to change and modify such rules from time to time upon reasonable notice to the public. Under its power to make rules it has been held that a railroad company could establish a station at which it would receive and store for shipment goods and merchandise, except coal, and fix an-

[53] Iron Mountain and So. Ry. v. Renfroe, 82 Ark. 145, (1907).
[54] Mich. Cent. R. R. Co. v. Smithson, 45 Mich. 212, (1881).

other place where it would receive coal for shipment, and the fact that a party had been in the habit theretofore of shipping coal at the same station where other goods were received, would not be a justification for his disregarding the rule of the railroad company, and insisting on continuing to ship coal from the general freight station.[55] A railroad company must in its own interest and the interest of the public, establish a schedule or time table for the running of its trains, and shippers of freight must make their shipments and so prepare their freight that it can be handled by the railroad company without undue loss of time and interference with the running of its trains, and it has been held that a railroad company was not bound to stop and hold its trains while four carloads of hogs were driven into its stock yard, and loaded into cars, counted, a way-bill made out, and a shipping contract signed.[56]

§ 45. Location of Stations. It is the duty of railroad companies to establish and maintain depots and stations for the comfort of passengers, and for the protection of shippers of freight at such points as will reasonably serve the public. Their location at points most desirable for the convenience of travel and business is alike indispensable to the efficient operation of the road and the enjoyment of it as a highway by the public. Necessarily the company cannot be required on the one hand, to locate stations at points where the cost of maintaining them will exceed the profits resulting therefrom to the company, nor allowed on the other hand, to locate them so far apart as to practically deny to communities on the line of the road reasonable access to its use. The duty to maintain or continue stations rests upon the same principle, and a company cannot, therefore, be compelled to maintain or continue a station at a point where the welfare of the company and the country in general require that it be changed to some other point.[57] In the absence of statutory provisions limiting and restricting

[55] Robinson v. B. & O. R. R. Co., 129 Fed. Rep. 754, (1904).
[56] Frazier & Cooper v. K. C., St. J. & C. B. Ry. Co., 48 Ia. 571, (1878).
[57] Mobile & Ohio R. R. v. People, 132 Ill. 559, S. C. 24 N. E. 643, (1890).

their powers, railroad companies are vested with a very broad discretion in the matter of locating and maintaining their freight and passenger stations. This discretion, however, is not absolute, but it is subject to the condition that it must be exercised in good faith, and with a due regard to the necessities and conveniences of the public. Railway companies though private corporations, are engaged in a business in which the public have an interest, and in which such companies are public servants, and amenable as such. In a case where it was shown that the citizens of a town of eighteen hundred inhabitants, with manufacturing and other business enterprises, and which was situated on the direct line of a railroad, were compelled to transport their freight and to travel by other means three and one-half miles either way to obtain shipping or traveling accommodations on said road, was held by the court to show such a disregard by the railroad of its duty to the public as to justify a court of equity by *mandamus* to require such railroad company to establish and maintain a station in such town for receiving and discharging both freight and passengers.[58] But it seems by the weight of authority, the location of stations is left to the discretion of the board of directors of the railroad company in the absence of statute. The location of stations on the part of the State is legislative and not judicial in its nature. In a case where a railroad had established stations at *A* and *B* and, thereafter, abandoned the station at *B* and established a station at *C*, beyond station *B*, and it was shown that the patronage of the road between *A* and *C* was insufficient to pay its running expenses for that part of the road, and to change the depots back to *B* would inconvenience a much larger part of the public than it would benefit, the Supreme Court of the United States refused to require the railroad company to re-establish its station at *B*.[59] In most of the States there are statutes authorizing the appointment of a Railroad Commission that usually, among a great many other duties and powers, has the duty

[58] People v. Chicago & Alton R. R., 130 Ill. 175, 22 N. E. 857, (1889).
[59] Nor. Pac. R. R. v. Washington, 142 U. S. 492, (1892).

and authority to require railroad companies to establish and maintain stations at places where they are needed by the public.[60]

§ 46. **Location of Switches.** A railroad company in its discretion may establish and discontinue switch connections with private warehouses and factories. The switch connection and transportation over it may seriously interfere with the convenience and safety of the public and with its use of the road, and it may embarrass the general business of the company. It is peculiarly within the discretion of the directors to determine whether it does or not. At one time in the life of the company it may be useful and consistent with all legitimate purposes of the company. A change of conditions, an increase in business, a necessity for travel at higher speed, may make such a connection either inconvenient or dangerous, or both, and justify the company in abandoning an established switch connection.[61] This discretion may be controlled by express statute, as in a case where the statutes of the State required a railroad company to deliver grain in bulk to the warehouses to which it is consigned if the road has connections with it.[62] The self interests of the railroad company will ordinarily cause the company to furnish sidetracks and switches where they are needed.

§ 47. **Duty to Deliver to Consignee.** It was the duty of common carriers at common law to deliver personally to the consignee, but the rule requiring goods to be delivered to the consignee personally at his place of business has been somewhat relaxed in favor of railroads on the ground that they have no means of delivery beyond their line. In cases where a shipment of goods is made to parties having switch connections with the line of the carrying road, it is the duty of the railroad company to make a personal delivery of the freight on his switch, and the common law is held to apply where the necessity for its relaxation does not

[60] Commissioners v. Portland & O. R. R. Co., 63 Me. 270.
[61] Jones v. Newport News & Miss. Valley Co., 65 Fed. Rep. 736, (1895).
[62] C. & N. W. R. R. Co. v. People, 56 Ill. 365, (1870).

exist. This rule has given rise to a classification of articles of freight with respect to delivery. Articles susceptible of easy transfer may be delivered at a general freight depot provided for that purpose, but live stock, coal, ore, grain, lumber, and the like belong to a different class. Persons engaged in receiving and forwarding this class of freight, such as manufactories consuming large quantities of heavy material, dealers in coal and grain, merchants receiving, storing, and forwarding grain in bulk usually select locations for the prosecution of their business adjacent to railroads, where they can have the benefit of side connections over which heavy freight can be delivered to them in bulk at their place of business. Railroad companies are bound to deliver and receive freight from sidetracks and switches where such are provided for that purpose. A railroad company will not be permitted to designate one place for its delivery of grain, and compel all those competing with the owner of such place to receive from, and transfer the grain through such selected elevator. If a railroad company possessed the right to refuse to deliver on such switches they could destroy one manufacturer and build up another, and exterminate or very materially cripple competition and, in a large measure, monopolize, and control these several branches of useful commerce, and dictate such terms as they might desire.

Absolute impartiality in serving their patrons is an imperative obligation of all railroad companies. In a case where *A* had a stock yard contiguous to a railroad depot and fitted it up with pens and stock gaps, connected with said road, appropriate for loading and unloading live stock, and there was thereafter a new stock-yards company organized and equipped, and the railroad company entered into an agreement with it agreeing to deliver to it all the live stock shipped or consigned to it for delivery in that town, and thereafter the railroad company refused to receive or deliver stock to *A* at his stock yards, the court held that it was the duty of the railroad company to deliver stock con-

signed to *A* at his stock yards, and to receive therefrom shipments of stock tendered by him.[63]

§ 48. **Special Charge for Delivering Freight.** Where a railroad company maintained connections with *A's* stock yards, and *B* was the proprietor of a yard for stock separated from *A* by only one street sixty feet in width, and both were equally well equipped for receiving, feeding, and caring for such stock as he purchased, or might be consigned to him for sale, and the railroad company entered into a contract with *A* to unload and load stock handled by it at his yards, making *A* the company's agent for the collection of freight charges, and *A* agreed to look after the stock that was unloaded in his yards for which he was to be paid by the shippers. It was held that when stock is offered to a carrier of live stock it is its duty to receive them. The duty to receive, transport, and deliver live stock cannot be fully discharged unless the carrier makes such provision at the place of loading as will enable it to properly receive and load the stock, and such provision at the place of unloading as will enable it to properly deliver the stock to consignee. But a carrier of live stock has no more right to make a special charge for merely receiving or merely delivering such stock, in and through a stock yards provided by itself, in order that it may properly receive and load or unload such stock, than a carrier of passengers to make a special charge for the use of its passenger depot by passengers when proceeding to or coming from its trains, or than a carrier to charge the shipper for the use of its general freight depot in merely delivering his goods for shipment or a consignee of such goods for merely receiving them there within a reasonable time after they are unloaded from the car. If a carrier may not make special charges in respect to stock yards which it owns, maintains, or controls, it cannot invest another corporation or company with authority to impose burdens of that kind upon shippers and consignees. The transportation of live stock begins with their delivery to the carrier to be loaded upon

[63] Coe v. Louisville & Nashville R. R. Co., 3 Fed. Rep. 775, (1880).

its cars, and ends only after the stock is unloaded and delivered, or offered to be delivered, to the consignee, if to be found, at such a place as admits of their being safely taken into possession. The carrier had no power to require the shipper to pay the favored stock yards for having its stock unloaded there.[64]

Right to Require All to Use One Stock Yards. A railroad company may require all shippers to use one designated stock yards company's yards, if consignees and shippers are permitted to use them without extra charge for merely delivering and receiving live stock.[65] In a New Jersey case a railroad company constructed a spur track along a public street and permitted manufacturers, coal dealers and the like to connect therewith by sidings, and *A* applied for a siding under the purpose of establishing a stock yards. The railroad company refused to permit him to do so on the ground that a stock yards was essentially different from the purpose to which the spur track was being devoted, and for the further reason that the railroad company had established connections with *B's* stock yards for the purpose of receiving and unloading stock, where no charge was made beyond the ordinary charge for transportation. It appeared that no charge was made for the loading or unloading of cattle at the stock yards, and after the cattle had been unloaded, and had not been taken away by consignee from the yard for two or three hours, they were then turned into the pens of the stock yards, where a charge of two dollars per car for a day or part of a day was made by the stock-yards company for keeping them, also a charge of five to ten cents per head. On these facts it was held that the contract between railroad company and the favored stock-yards company for the use of its chutes to unload and receive live stock at that point, as its station for unloading and loading live stock without any yardage charge or fee for the proper loading and unloading of cattle

[64] Covington Stock Yards Co. v. Keith, 139 U. S. 128, (1891).

[65] Butchers & Drovers Stock Yards Co. v. L. & N. R. R., 67 Fed. Rep. 35, (1895).

was proper, and that were the railroad company the owner of the stock yards, it would have the right to impose a charge for delay of the consignee in keeping his stock beyond two hours after unloading, and that it was not unreasonable for the railroad company to permit its agent, the stock-yards company, to make such a reasonable charge for turning the cattle into its pens and keeping them there after such a delay, that the railroad company, by delivering the cattle to the stock-yards company, to keep until the appearance of the consignee, could incur only a reasonable charge for the keeping of the cattle and that in any event the stock-yards company at common law was confined to a reasonable charge for its services, because of the public nature of the business in which it was engaged.

§ 49. Excuses for Not Receiving Freight. A common carrier of freight is bound to receive all merchandise offered for shipment, unless the condition or character of the goods offered is such as to impose an extra hazardous undertaking, but the objection to be valid must arise out of the goods and not the shipper. The goods when offered, must be packed in such a manner as to make them in reasonably safe condition for shipment. And the carrier cannot impose unreasonable conditions as to packing, in order to compel the shipper to sign a release, discharging the railroad from liability for loss or damage to such goods. Thus the fact that there had been many disputes, resulting in seven or eight lawsuits between a shipper and the railroad company, was held to be no excuse justifying the railroad company to refuse to receive freight for shipment from him.[66]

§ 50. Dispute between Railroad Company and Employes. A railroad company cannot refuse to furnish shipping facilities for shipping freight, merely because a part of its employes have quit its service on account of a disagreement about wages. In a case where for two weeks a railroad company had refused to receive large quantities of goods offered for transportation, and had closed its

[66] Lanning v. Sussex Ry. Co., 1 N. J. Law Journal 21, (1877).

gates during business hours because the skilled freight handlers employed by the railroad who had been working at the rate of seventeen cents per hour, refused to work unless twenty cents per hour were paid, and had abandoned their work, and the delay was caused by the inefficiency of the unskilled men, the court said:

"It appears that a body of laborers in concert fixed a price for their labor, and refused to work at a less price. The railroad company fixed a price for the same work and labor, and refused to pay more. In doing this neither did any act in violation of any law, nor subjected either to any penalty. The railroad company had a right to take their ground in respect to the price to be paid and adhere to it if they chose; but if the consequence of doing so was an inability to exercise their corporate franchise to the great injury of the public, they cannot be heard to assert that such consequence must be shouldered and borne by the public, who neither directly nor indirectly participated in their causes. If it had been shown that a 'strike' of their skilled laborers had been caused or compelled by some illegal combination or organized body, which held an unlawful control of their actions, and sought through them to enforce its will upon the respondents, and that the respondents, in resisting such unlawful efforts, had refused to obey unjust and illegal dictation, and had used all the means in their power to employ other men in sufficient numbers to do the work, and that the refusal and neglect complained of had grown out of such a state of events, a very different case for the exercise of the discretion of the court would have been presented. The most that can be found from the petition and affidavits is that the skilled freight handlers of the railroad company refused to work without an increase of wages to the amount of three cents per hour. The railroad company refused to pay such increase. The laborers then abandoned the work, and the railroad company did not procure other laborers competent or sufficient in number to do the work. These facts reduce the question to this: Can railroad corporations refuse or neglect to perform their public duties upon a controversy with their employees over the cost or expense of doing them? We think this question admits of but one answer. The excuse has in law no validity. The duties imposed must be discharged at whatever cost. They cannot be laid down, or

abandoned, or suspended without the legally expressed consent of the State. The trusts are active, potential, and imperative, and must be executed until lawfully surrendered, otherwise a public highway of great utility is closed or obstructed without any process recognized by law." [67]

§ 51. Public Duties of Employes of Railroad Company. A railroad employe, when he accepts employment from one engaged in such a business, owes to such railroad company and to the public a higher duty than though his service had been due to a private person. He enters the company's service with full knowledge of the exacting duties owed the public. He knows that if the company fails to comply with the law in any respect severe penalties and losses will follow for such neglect. An implied obligation is, therefore, assumed by such employes on accepting service from it that they will perform their duties in such manner as to enable the company to discharge its obligations faithfully, and also to protect it against irreparable losses and injuries, and excessive damages by any acts or omissions on their part. One of the implied conditions on their behalf is that they will not leave its service, or refuse to perform their duties under circumstances when such neglect on their part would imperil lives committed to its care, or the destruction of property involving irreparable losses and injury, or visit upon it severe penalties. In ordinary conditions, as between employer and employe, the privilege of the latter to quit the former's service at his option cannot be prevented by restraint or force. The remedy for breach of contract may follow to the employer, but the employe has it in his power to arbitrarily terminate the relation, and abide the consequences. But these relative rights and powers may become quite different in the case of the employes of a great public corporation, charged by the law with certain great trusts and duties to the public. An engineer and a fireman who start from Toledo with a train of cars filled with passengers, destined for Cleveland, begin that journey under contract to drive their engine

[67] People v. N. Y. C. R. R. Co., 28 Hun 543, (1883).

and draw the cars to the destination agreed upon. While it is plain that this engineer and fireman could quit their employment when the train is part way on its route, and abandon it at some point where the lives of the passengers would be imperiled and the safety of the property jeopardized, the simple statement of the proposition carries with it its own condemnation. The very nature of their service, involving as it does the custody of human life, and the safety of millions of dollars' worth of property, imposes upon them obligations and duties, commensurate with the character of the trusts committed to them. They represent a class of skilled laborers, limited in number, whose places cannot always be supplied. These cars carry supplies and material upon the delivery of which the labor of tens of thousands of mechanics is dependent. They transport the products of factories whose output must be speedily carried away to keep their employes in labor. The suspension of work on the line of such a vast railroad, by an arbitrary action of the body of its engineers and firemen, would paralyze the business of the entire company, entailing losses and bringing disaster to thousands of unoffending citizens. Contracts would be broken, perishable property destroyed, the traveling public embarrassed, injuries sustained, too many and too vast to be enumerated. If such ruin to business of employers, and such disasters to thousands of the business public, who are helpless and innocent, is the result of conspiracy, combination, intimidation, or unlawful acts of organizations of employes, the courts have the power to grant partial relief, at least by restraining employes from committing acts of violence or intimidation, or from enforcing rules and regulations of organizations which result in irremediable injuries to their employers and the public.[68]

§ 52. Contracts Destroying Competition. A railroad company owes the duty to the public to afford reasonable facilities for the transportation of persons and property, and to charge only reasonable rates for such service. Any

[68] Toledo, A. A. & N. M. Ry. Co. v. Penn. Co., 54 Fed. Rep. 746, (1893).

contract which disables it from performing these duties, or which makes it to its interest not to perform them, or removes all incentive to their performance, is contrary to public policy, and void. In a case where a contract was entered into by seven railroads by the terms of which all their roads were to be operated, as to through traffic, as if operated by one corporation which owned all of them, and which provided for a division of such traffic, and where this was not done, for a division of the gross earnings of the seven roads, it was held that this contract removed every incentive to the railroad companies to afford the public proper facilities and to carry at reasonable rates, because under its provisions each company was entitled to its full percentage of all earnings, even though it did not carry a pound of freight. The necessary, inevitable result of such a contract was to foster and create poor service and higher rates. There is no inducement for a road to furnish good service and carry at reasonable rates, when it receives as much or more for poor service or for no service, as it would receive for good service and an energetic struggle for business, and that since the obvious purpose of this contract was to suppress or limit competition between the contracting companies in respect to the traffic covered by the contract, without regard to the question of their reasonableness, it is, therefore, contrary to public policy and void.[69]

§ 53. Railroad Companies as Trustees. The rule that public service corporations are trustees of the powers granted to them, and that they hold such powers for the purpose of rendering service to the public, and will not be permitted to put themselves in such a position as to make their own interests adverse to the public interests, has been embodied in the Act of Congress to regulate interstate commerce. The Supreme Court, through Justice White, in construing the Act, said:

"We then construe the statute as prohibiting a railroad

[69] C. M. & St. P. R. R. v. Wabash, St. L. & P. R. R., 61 Fed. Rep. 993, (1894).

company engaged in interstate commerce from transporting in such commerce articles, or commodities under the following circumstances and conditions: (a) When the article or commodity has been manufactured, mined, or produced by a carrier under its authority, and at the time of transportation, the carrier has not, in good faith, before the act of transportation, dissociated itself from such article or commodity; (b) when the carrier owns the article or commodity to be transported, in whole or in part; (c) when the carrier, at the time of transportation, has an interest direct or indirect, in a legal or equitable sense, in the article or commodity, not including, therefore, articles or commodities, manufactured, mined, produced, or owned, by a *bona fide* corporation in which the railroad company is a stockholder." [70]

[70] U. S. *ex rel.* v. Del. & Hud. R. R. Co., 29 Sup. Ct. Rep. 527, (1909).

CHAPTER III

PUBLIC REGULATION OF RAILROAD RATES

§ 54. Basis of Right to Regulate. The Supreme Court of the United States has said:

"That railroads from the public nature of the business by them carried on, and the interest which the public has in their operation are subject as to their State business, to State regulations, which may be exercised either directly by legislative authority or by administrative bodies endowed with power to that end."

This power embraces the railroad business in its entirety and extends to all matters connected therewith affecting its duty to the public.[1] It will be noticed that the right to regulate is based by the Supreme Court on the nature of the calling. From this it is evident that a like power can be exercised as to all other public callings.

The power to grant to public service corporations the right of eminent domain is also based upon the same grounds, and the fact that such a corporation in pursuance of such a grant exercises the power so granted is by many courts assigned as additional grounds for regulation upon the part of the public. The right of eminent domain can be used only when the public good requires, and therefore, when this power is delegated, the Government must still control by regulation.

§ 55. Eminent Domain. The right of eminent domain

[1] Atlantic Coast Line R. R. v. N. Car. Corporation Commission, 206 U. S. p. 1, (1907).

is the power to take private property for public use. This power belongs to every independent government. It is an incident to sovereignty and requires no constitutional recognition. The provisions in the constitution of the several States, for just compensation for property taken, is merely a limitation upon the use of the power. With this limitation added it is the power to take private property, not by the consent of the owner, but without his consent upon payment of the market price. When the use to which the property taken is to be applied is public, the propriety or the expediency of the appropriation by the legislature cannot be called in question by any other authority. The proceedings for ascertaining the value of the property and the consequent compensation to be made is merely an inquisition to establish the value, in compliance with the constitutional requirements, preliminary to the actual taking, and it may be prosecuted before commissioners, or special boards, or the courts, with or without the intervention of a jury, as the legislative power may designate.[2] This power may be granted by the legislature to anyone who is engaged in the performance of a public service and who in the discharge of such service will need to exercise the power. When a particular corporation or individual claims the right to take property without the consent of the owner it must show not only a legislative grant, but it must be able to establish the fact that the enterprise in which it is engaged is one by which a public use or benefit is to be subserved or promoted, so that such a taking can be said to be for a public and not a private use. The necessity or expediency of taking private property for public use, the instrumentalities through which it may be done, and mode of procedure are legislative and not judicial questions. But whether the proposed use is in fact public, so as to justify its taking without the consent of the owner, has always been a question for the courts to determine. In doing so they are not confined to the description of the objects and

[2] U. S. v. Jones, 109 U. S. 513.

purposes of the corporation as set forth in its articles of incorporation, but may resort to an investigation showing the actual business proposed to be conducted by it.[3] What is a public use may frequently and largely depend upon the facts surrounding the subject.[4] All corporations that are recognized as being engaged in a public business may, when granted that right by the legislature, either by special act or general law, exercise the right. In the case of railroads the question of public use is determined by the fact that the road is intended as a highway for the use of the public in the transportation of freight and passengers, and it can make no difference that its use may be limited by circumstances to a small part of the community. Its character is determined by the right of the public to use it, and not by how many will use it.[5]

§ 56. Fixing of Rates a Legislative Function. The fixing of charges for the transportation by a common carrier of persons or property is a legislative and not a judicial function. But it is competent for the courts, in the absence of legislative regulations, to protect the public against the exaction of oppressive and unreasonable charges.[6] Under the common law, if a carrier attempted to charge a shipper an unreasonable sum, the courts had jurisdiction to inquire into the matter, and to award the shipper any amount exacted from him in excess of reasonable rates, and also in cases where a shipper refused to pay a reasonable rate the courts would render judgment in favor of the carrier for the amount found to be a reasonable charge. The province of the courts has not changed, nor the limit of the inquiry altered, because the legislature instead of the carrier prescribes the rates. The courts are not authorized to reduce or change the schedule of rates imposed by the legislature or a commission. They do not determine whether one rate is preferable to another, or what under all circumstances would be fair and reasonable between a carrier and ship-

[3] Bridal Veil Lumbering Co. v. Johnson, 30 Ore. 205, (1896).
[4] Clark v. Nash, 198 U. S. 361.
[5] DeCamp v. Hibernia R. R. Co., 47 N. J. Law 43.
[6] Griffin v. Goldsboro Water Co., 112 N. C. 206, (1898).

per; they do not engage in merely administrative work of any kind.[7] In a case where a complaint was presented to the court alleging that the rates of a water company were too high, but failing to specify any particular charges as being excessive, a decree of the court based thereon, fixing a schedule of prices covering all the business of the company, was set aside as being beyond the prerogative of the court.[8]

To determine the question whether such rates are reasonable or unreasonable is a judicial function. The courts investigate the reasonableness of such charges solely for the purpose of determining whether, under the provisions of the Constitution, the rates fixed amount to a taking of property on the part of the State without due process of law, or to a denial to such railroad company of the equal protection of the laws.

§ 57. Judicial Duties in Regard to Rates. The rates of charges made by a public service corporation fixed by the legislature or by a commission must be reasonable. The only function of the courts in the matter of rates fixed by commissioners is to determine whether the rates fixed violate this constitutional provision. It was said by the Supreme Court of Minnesota, in passing upon a schedule of charges fixed by the State Commission of that State, that courts should be very slow to interfere with the deliberate judgment of the Legislature or of a Legislative Commission in the exercise of what is confessedly a legislative or administrative function. To warrant such interference it should clearly appear that the rates fixed are so grossly inadequate as to be confiscatory, and hence in violation of the Constitution. It is not enough to justify the court in holding a rate unreasonable, and hence unconstitutional, that, if it was its province to fix rates, it would in its judgment have fixed them somewhat higher. Any such doctrine would result in effect, in transferring the power of fixing rates from the legislature to the courts, and making it a

[7] Reagan v. Farmers Loan & Trust Co., 154 U. S. 362.

[8] Brymer v. Butler Water Co., 179 Pa. State 231, (1897).

judicial and not a legislative function. When there is room for a reasonable difference of opinion, in the exercise of an honest and intelligent judgment, as to the reasonableness of a rate, the courts have no right to set up their judgment against that of the legislature or of a Legislative Commission.[9]

§ 58. Force of Rates Fixed by Commission. The presumption is that the rates fixed by the commissions created by the States or by the United States are reasonable, and the burden of proof is upon the railroad companies to show the contrary. In a case where a State Railroad Commission reduced the freight on a single article (phosphate), the Supreme Court of the United States refused to set it aside because the railroad company failed to produce any evidence to show that the rate so fixed was unreasonable, saying:

"There is no evidence of the amount of phosphates carried locally; neither is it shown how much a change in the rate in carrying phosphates will affect the income of the companies. There is testimony tending to show the gross income from all local freights and the value of the railroad property, and also certain difficulties in the way of transporting phosphates owing to the lack of facilities at the terminals. We are aware of the difficulty which attends proof of the cost of transporting a single article, and in order to determine the reasonableness of a rate prescribed it may sometimes be necessary to accept as a basis the average rate of all transportation per ton per mile." [10]

In another case involving the same rate it was shown that the rate as fixed by the commission on phosphates was higher than the average freight rate per ton per mile in that State, and upon that showing the Supreme Court refused to interfere with the rate.[11]

§ 59. Classes of Public Service Corporations. In the matter of fixing rates there is a distinction more or less clearly recognized by courts and commissions, between cor-

[9] Steenerson v. Great Northern Ry. Co., 69 Minn. 353, (1897).
[10] Atlantic Coast Line Co. v. State of Florida, 203 U. S. 256, (1906).
[11] Seaboard Air Line Ry. v. State of Florida, 203 U. S. 261.

porations that are distinctly public agents and necessarily exercise public franchises and intend to render public service, such as railroads, and those corporations which, without any intent of public service, have placed their property in such a position that the public has an interest in its use, such as grain elevators. In the case of railroads the corporation has intentionally devoted its property to the discharge of a public service and generally exercises some of the governmental powers, such as the power of eminent domain. Public service companies, such as grain elevators, and stock yards, and the like, are not doing the work of the State and are not using their property in the discharge of a purely public service, and they usually do not require a grant of any one of the State's governmental powers.[12] In the case of distinctly public agencies the basis of the charge should be a reasonable return on the value of the property used by the corporation in the service of the public, while in the case of private employments in which the public has an interest, the basis of the charge should be the value of the service to the one receiving it. In a case where a State statute fixed the limit of the amount to be charged by stock yards, based on the volume of business only, it was held that the statute was unconstitutional and the Supreme Court of the United States in its decision said:

"That the State's regulation of the charge of such a company should not be measured by the aggregate of its profits, determined by the volume of its business, but by the question whether any particular charge to an individual dealing with it was, considering the service rendered, an unreasonable charge. In other words, if such a company has a thousand transactions a day, and its charges in each are but a reasonable compensation for the service received by the party dealing with it, such charges do not become unreasonable because, by reason of the multitude of transactions, the aggregate of his profits is large. The question is not how much he makes out of the volume of his business, but whether in each particular transaction the charge is an

[12] Smyth v. Ames, 169 U. S. 466, (1898).

unreasonable exaction for the services rendered. Such companies have a right to charge for each separate service that which is a reasonable compensation therefor, and the legislature cannot deny to them such reasonable compensation and cannot interfere simply because out of the multitude of its transactions the amount of its profits are large." [13]

It was held in a suit involving the question as to what was a reasonable charge for the use of a bridge, that the question was not what profit it may be reasonable for the bridge company to make, but what is reasonable to charge to the person to whom the service is rendered and who is charged.[14]

§ 60. **Determining Reasonable Rates.** A railroad company is entitled to ask a fair return upon the value of the property which it employs for the public convenience. Just compensation is a fair return upon the reasonable value of the property at the time it is being used for the public. In order to ascertain that value, the original cost of construction, the amount expended in permanent improvements, the amount and market value of its stocks and bonds, the present, as compared with the original cost of construction, the probable earning capacity of the property under rates prescribed by statute, the sum required to meet operating expenses, are all matters of consideration, and are to be given such weight as will be just and right in each case.[15] Profits should not be allowed on fictitious capitalization, or interest on bonds issued in an amount in excess of the value of the road. Expenditures for additions to the construction and equipment should be distributed *pro rata* over the period of the life of such additions, and should be reimbursed by all of the traffic they accommodate during the period of their duration, and improvements that will last many years should not be charged

[13] Cotting v. Goddard, 183 U. S. 79, (1901).

[14] Canada So. Ry. Co. v. International Bridge Co., L. R. 8 App. Cas. 723, (1883).

[15] Smyth v. Ames, 169 U. S. 466, (1898).

wholly against the revenue of a single year.[16] The liability of common carriers as insurers must be taken into account in fixing a schedule of rates. A higher rate should be fixed for valuable articles than those of lesser value. In a case where the Interstate Commerce Commission fixed a freight rate for window shades, and did not discriminate between such as were worth three dollars per dozen, and those worth ten dollars per pair, the rate was held invalid because it did not allow the carrier any compensation for the additional risk.[17]

§ 61. General Power of Public to Fix Rates. The State has power to fix the maximum charges that shall be made by railroad companies for the transportation of persons and property within its own jurisdiction, unless restrained by valid contract with such companies. But under the pretense of regulating and fixing fares and freights, the State can not require a railroad company to carry persons or property for less than reasonable rates. On the subject of the right on the part of the State to regulate railroads the United States Supreme Court has said that:

"A corporation maintaining a public highway, although it owns the property it employs for accomplishing public objects, must be held to have accepted its rights, privileges, and franchises, subject to the condition that the government creating it, or the government within whose limits it conducts its business, may by legislation protect the people against unreasonable charges for the service rendered by it. It can not be assumed that any railroad corporation, accepting franchises, rights, and privileges at the hands of the public, ever supposed that it acquired, or that it was intended to grant to it, the power to construct and maintain a public highway simply for its benefit, without regard to the rights of the public. But it is equally true that the corporation performing such public services and the people financially interested in its business and affairs, have rights that may not be invaded by legislative enactment in disregard of the fundamental guarantees for

[16] Ill. Cent. R. R. Co. v. Interstate Commerce Commission, 206 U. S. 441, (1907).

[17] Interstate Com. Comm. v. Del. Lack. & West. Ry. Co., 64 Fed. 723, (1894).

the protection of property, contained in the Fourteenth Amendment to the Constitution of the United States, prohibiting the States from depriving any person of his property without due process of law, or denying to any one the equal protection of the laws. It has been held that corporations are persons within the purview of this section, and if a State fixes railroad rates so low as to prevent them from receiving a reasonable return on the investment, it amounts to a depriving them of their property without due process of law and a denial of equal protection of the laws. The corporation can not be required to use its property for the benefit of the public without receiving a just compensation for the services rendered by it." [18]

§ 62. **Intrastate Rates.** A majority of the States have enacted laws providing for the appointment of commissions whose duties and powers are generally fixed and determined by the statutes creating the commission, but since the right to regulate interstate commerce is vested solely in Congress, a State must confine its fixing of rates to the rates charged for intrastate or domestic business. In the case of State v. Smyth, the Supreme Court of the United States said:

"In our judgment, it must be held that the reasonableness of rates prescribed by a State for the transportation of persons and property wholly within its limits must be determined without reference to the interstate business done by the carrier, or to the profits derived from it. The state can not justify unreasonably low rates for domestic transportation, considered alone, upon the ground that the carrier is earning large profits on its interstate business, over which, so far as rates are concerned, the State has no control. Nor can the carrier justify unreasonably high rates on domestic business upon the ground that it will be able only in that way to meet losses on its interstate business; nor the latter the losses on domestic business. It is only rates for the transportation of persons and property between points within the State that the State can prescribe; and when it undertakes to prescribe rates not to be exceeded by the carrier, it must do so with reference exclusively to what is just and reasonable, as between the car-

[18] Smyth v. Ames, 169 U. S. 466, (1898).

rier and the public, in respect of domestic business. The argument that a railroad line is an entirety; that its income goes into, and its expenses are provided for, out of a common fund; and that its capitalization is on its entire line, within and without the State, can have no application where the State is without authority over rates on the entire line, and can only deal with local rates, and make such regulations as are necessary to give just compensation on local business."[19]

§ 63. Extent of Power of State Railroad Commissions. The general business management of a railroad company is in the hands of its board of directors, the same as that of other business corporations, and the State has in general no right to interfere with its internal management, such as to fix wages of employes, or control its contracts for construction, or the purchase of its supplies. It has the clear right, however, to pass upon the reasonableness of contracts in which the public is interested, whether such contracts be made with particular patrons of the road, or they be made between several railroads providing for joint action in the transportation of persons or property. In a case where two or more roads had entered into a joint-rate agreement it was held that such joint rate might be reduced by a Railroad Commission.[20] It was further held in said case that such a Commission, in exercising its powers of supervision of such rates, is not bound to reduce the rate upon all classes of freight, and if upon examination of tariffs of a certain road, the Commission is of the opinion that the rate on a particular article or class of freight is disproportionately or unreasonably high, it may reduce such rate, notwithstanding that it may be impossible for the company to determine with mathematical accuracy the cost of transportation of that particular article as distinguished from all others, and such a reduction can not be shown to be unreasonable, simply by proving that if applied to all classes of freight it would result in unreasonably low rates. It sometimes happens that for pur-

[19] Smyth v. Ames, 169 U. S. 466, (1898).

[20] Minn. & St. L. R. R. Co. v. State of Minn., 186 U. S. 257, (1902).

poses of ultimate profit and for building up a future trade, railways carry both freight and passengers at a positive loss, and while it may not be within the power of the Commission to compel such a tariff, it cannot, upon the other hand, be claimed that the railroad can in all cases be allowed to charge grossly exorbitant rates on other articles, as compared with rates paid upon other roads, in order to pay dividends to stockholders.

§ 64. Regulations Other than Fixing of Rates. The power to regulate extends to the business in its entirety, as far as the public are interested therein. It includes the power to require carriers to make reasonable connections with other roads, so as to promote the convenience of the traveling public. The prime duty of a carrier is to furnish adequate facilities to the public, and a State Commission may compel a railroad company to perform this duty, although by doing so it may cause incidental loss to the company in rendering such service. The performance of such a duty does not in and of itself, give rise to the conclusion of unreasonableness, as where it was held that although compliance with the order made necessary the operation of an extra train at a loss, so long as the income of the railroad company from all its business in the State affords adequate remuneration.[21] And further, it is within the province and power of a State to create a Commission with authority to compel railroads to make track connections at the intersection of other roads for transferring cars from the tracks of one company to those of another, and for the interchange of cars and traffic between their lines, even though the railroad company, in carrying out the order, would be required to expend some money and resort to the exercise of the power of eminent domain.[22]

§ 65. Purposes of the Interstate Commerce Act. Justice Brown, speaking for the United States Supreme Court, sets out the purposes of the Interstate Commerce Act as follows:

[21] Atl. Coast Line R. R. v. N. Car. Corp. Comm., 206 U. S. 1, (1907).
[22] Wisc. M. & P. R. R. Co. v. Jacobson, 179 U. S. 287.

"The principal objects of the Interstate Commerce Act were to secure just and reasonable charges for transportation; to prohibit unjust discrimination in the rendition of like services under similar circumstances and conditions; to prevent undue or unreasonable preferences to persons, corporations, or localities; to prohibit greater compensation being charged for a shorter than for a longer distance over the same line; and to abolish combinations for the pooling of freights. It was not designed, however, to prevent competition between different roads, or to interfere with the customary arrangements made by railway companies for reduced fares in consideration of increased mileage, where such reduction did not operate as an unjust discrimination against other persons traveling over the road. In other words, it was not intended to ignore the principle that one can sell at wholesale cheaper than at retail. It is not all discriminations or preferences that fall within the inhibition of the statute; only such as are unjust or unreasonable. For instance, it would be obviously unjust to charge *A* a greater sum than *B* for a single trip from Washington to Pittsburg; but, if *A* agrees not only to go, but to return by the same route, it is no injustice to *B* to permit him to do so for a reduced fare, since the services are not alike, nor the circumstances and conditions substantially similar. Indeed, the possibility of just discriminations and reasonable preferences is recognized by the Act, in declaring what shall be deemed unjust."

In applying these principles it was held that it was not a violation of the Act for a railroad company to sell a party rate ticket covering the transportation of ten or more persons, from one place to another, at less than the regular passenger rates for such passage, because such a sale did not operate to the prejudice of a single passenger, and all railroads had the same right to issue them to compete for the same traffic.[23] It has further been held by the United States Supreme Court that an allowance for cartage made by a railroad company to a shipper who had no siding connection with that line—although he had such connection with another competing line—was in violation of the Interstate Commerce Act prohibiting rebates and special

[23] Interstate Com. Comm. v. Balt. & Ohio R. R. Co., 145 U. S. 263, (1892).

rates, when a similar allowance was not made to another person who shipped goods over the same line under the same circumstances, except that he had no siding connection with either road.[24] And it was further held that the furnishing of free cartage for delivery of goods at one town but not at another, to which the same rates were charged for a shorter haul, was not an unjust discrimination in rates.

§ 66. **Basis of Proper Discrimination.** Common carriers whether engaged in interstate commerce or that wholly within a State, are performing a public service. They are usually endowed by the State with the right of eminent domain, and are so endowed to enable them more effectually to carry out the public service they undertake to render. As a consequence of this all individuals have equal rights, both in respect to service and charges. Such equality of right, however, does not prevent differences in the modes and kinds of service, and different charges based thereon. There is no cast iron rule of uniformity which prevents a charge from being above or below a particular sum, or requires that the service shall be exactly along the same lines. The principle of equality forbids any difference in charge which is not based upon difference of service. Any difference in charge must have some reasonable relation to the amount of difference in service, and can not be so great as to amount to an unjust discrimination.[25] Where *A* and *B* were both dealers in coal in the same market, the giving of a reduced rate to *A* was held to be an unjust discrimination.[26] A railroad company has no power to designate who shall deliver freight to it. It thereby places an additional burden upon the shippers. In a case where a railroad corporation owning a dock refused to receive coal on its cars at said dock from a canal boat, unless the owners of the canal boat would employ certain shovelers furnished by the railroad company at a price

[24] Wight v. U. S., 167 U. S. 512, (1897).
[25] W. U. Tel. Co. v. Call Pub. Co., 181 U. S. 92, (1901).
[26] Goodridge v. Union Pac. Ry. Co., 37 Fed. Rep. 182, (1889).

fixed by the company, to shovel the coal on board of the canal boat into tubs belonging to the company, which were then to be hoisted by means of a derrick on the dock and the coal dumped into the cars; it was held that such was an unreasonable requirement and could not be enforced by the railroad company,[27] because it burdened shippers with a charge in addition to the freight rate.

§ 67. **Common Law as to Discrimination.** At common law a common carrier was always entitled to a reasonable compensation for his services, hence it follows that he is not required to treat all those who patronize him with absolute equality. It is his privilege to charge less than a fair compensation to one person, or to a class of persons, and others cannot justly complain as long as he carries on reasonable terms for them. Respecting preferences in rates of compensation his obligation is to charge no more than a fair return in each particular transaction, and except as thus restricted, he is free to discriminate at his pleasure. This is equal justice to all which is all that the common law expects from the common carrier in his relation to the public.

§ 68. **Discrimination under Statutes.** Railroad companies are engaged in a business in which the public are interested, and the duties and obligations growing out of it may be enforced through the courts and the legislative power. These duties are to a great extent regulated by statute in most of the States, and so far as they enter into the business of interstate commerce by an Act of Congress, railroad companies regulated by the principles of common law, were required to carry for all persons who applied, in the order in which the goods were delivered at the particular station, and their charges for transportation were required to be reasonable, and by weight of authority their charges were required to be equal to all persons for similar services. To prevent discrimination and to secure uniformity of rates, and fix reasonable charges, statutes have been passed in most of the States providing means for the

[27] 318½ Tons of Coal, 14 Blatchford 453, 23 Fed. Cas. 1163, (1877, 1878).

investigation and control of railroads, as to their various duties to the public.

Permissible Discrimination. Harmless discriminations may in general be made by railroads. The carrying free of one person who is unable to pay fare, is no injustice to passengers who may be required to pay the reasonable and regular rates fixed by the company. Freight carried over long distances may be carried at a reasonably less rate per mile than the freight transported for shorter distances, because it costs proportionately less to perform the service. Passengers may be divided into different classes, and the fare regulated in accordance with the accommodations furnished to each, because it costs less to carry an emigrant with the accommodations furnished to that class, than it does to carry an occupant of a parlor car. And likewise an inferior class of freight may be carried at a less rate than first class merchandise of greater value and requiring more labor, care, and responsibility in handling. Twenty separate parcels done up in one package and consigned to the same person, may be carried at a less rate per parcel than twenty parcels of the same character consigned to as many different persons at the same destination, because it costs less to receive and deliver one package containing twenty parcels to one individual than it does to receive and deliver twenty different parcels to as many different consignees. In a case where a railroad company made a difference between the freight rates charged to small and large shippers, in favor of the large shippers, without reference to any conditions tending to decrease the cost of transportation, it was held to be an unjust discrimination prohibited by law.[28]

[28] Hayes v. Penn. Co., 12 Fed. Rep. 309, (1882).

CHAPTER IV

SPECIFIC DUTIES AND LIABILITIES OF COMMON CARRIERS OF GOODS

§ 69. Extent of Liability. The general rule is that a carrier is liable in all cases, excepting the loss occasioned by the Act of God, or the king's enemies. But whether they are liable for the loss of particular goods intrusted to them for carriage depends upon the nature and extent of the employment, express or implied, which the carrier is engaged in. Carriers may be employed in the transportation of goods and merchandise generally, and when so engaged they are bound to the common duties, obligations, and liabilities of common carriers. The employment may be limited to the mere carriage of particular kinds of property and goods; and when this is so, and the fact is known and avowed, the carrier will not be liable as a common carrier for any other goods or property intrusted to their agents without their consent. The transportation of passengers, or of merchandise, or of both does not necessarily imply that the owners hold themselves out as common carriers of money or bank bills. The owners of stage coaches whose ordinary employment is limited to the transportation of passengers and their baggage, would not be liable for parcels of goods or merchandise intrusted to the drivers employed by them. In all cases the nature and extent of the employment or business which is authorized by the owners and which, expressly or impliedly, they hold themselves out as undertaking, furnishes the true limits of their rights, obligations, duties, and liabilities. And further, no person is a common carrier in the sense of the law who is not a carrier for hire.[1] However, the contract of carriage does not imply a personal trust which can be

[1] Citizens Bank v. Nantucket Steamboat Co., U. S. Cir. Ct., 2 Story 16, (1811).

executed only by the contracting party himself, or under his supervision by agents and means of transportation directly and absolutely within his control. The particular mode or agency by which the service is to be performed, does not enter into the contract of carriage with the owner or consignor, and there is no distinction in the nature and extent of the liability attaching to carriers as between those who undertake to transport property by the employment of other common carriers, such as express companies, and those performing a like service through means under their own personal control.[2]

§ 70. When Liability Attaches. In order to render a party liable as a common carrier for the transportation of property it is necessary that it be delivered to and accepted by him for that purpose, but such acceptance may be either actual or constructive. The general rule is that it must be delivered into the hands of the carrier himself and if it is merely deposited in the yard of an inn, or upon the wharf to which the carrier resorts, or is placed in the carrier's cart, vessel, or carriage without the knowledge and acceptance of the carrier, his servants or agents, there will be no such delivery of the property as to create the responsibility of a common carrier therefor; the carrier and shipper may make such stipulations on the subject as they see fit, and such special arrangement, when made, will govern. If, therefore, they agree that the property may be deposited for transportation at any particular place and without any express notice to the carrier, such deposit merely will be a sufficient delivery. And even a constant and habitual practice and usage on the part of the carrier to receive property for transportation, in a certain manner, and without any special notice may make a delivery of property at such place a sufficient delivery for the purpose of placing responsibility upon the carrier.

Illustrations. In a case where a truckman took an engine to a freight station for the purpose of transportation, and the agent directed that the engine be placed near a certain

[2] Buckland v. Adams Ex. Co., 97 Mass. 124, (1867).

derrick, which was done, and the employes of the railroad in loading the engine injured it, it was held that the liability of the railroad as a common carrier had attached.[3] Where a lighter was sent to the wharf to take goods to a larger vessel, and the goods were lost from the lighter, it was held there was sufficient delivery and acceptance to make the owner of the larger vessel liable as a common carrier.[4] Where wheat was being delivered into a vessel for shipment by means of a pipe, and the vessel turned so as to open the pipe and some of the wheat was lost, it was held that there was a delivery of the wheat as fast as it went into the vessel.[5]

§ 71. Change of Liability from Warehouseman's to Common Carrier's. The freight depots of railroad corporations are commonly used for a double purpose, one is for keeping goods that are brought there for immediate transportation, and also to store goods transported to them on the railroad for immediate delivery to the consignee. The other is, for warehouses for the storage of goods brought there for carriage at some future time, and also of goods brought to them by the railroad but to be delivered to the consignee at some future time, after the duties of the company as carriers have ceased. In respect to goods received, their liability as carriers begins as soon as the duty of immediate transportation arises, but not while they are delayed for the convenience of the owner. Sometimes articles are transported in carload lots which are delivered at the depot on different days and in small quantities, and are kept there until one or more carloads are collected. In such a case the liability does not arise until the goods are all delivered and ready for transportation. In a case where a manufacturer of corn planters was shipping a lot of one thousand corn planters, and nine hundred were taken to the freight depot, and thereafter the depot was destroyed by fire, it was held that the liability of the railroad com-

[3] Merritt v. Old Colony & Newport Ry. Co., 11 Allen 80, (1865).
[4] Buckley v. Naumkeag Steam Cotton Co., 24 Howard 386, (1860).
[5] R. G. Winslow, 4 Biss. 13, (1860).

pany as common carrier was to be determined by the fact as to whether there was an order for the railroad company to ship the planters as they were delivered, or the planters were all to be shipped in one shipment.[6]

§ 72. Bailment and Degrees of Care. A bailment has been defined to be "the delivery of a thing in trust for a particular object or purpose, expressed or understood, and upon a contract, express or implied, to conform to that object or purpose."[7] The term applies to the relation created where one person's goods are left with another, as where one leaves his watch with a jeweler to be repaired, the transaction is one of bailment. The jeweler is called the bailee and the owner the bailor. The contract between a shipper and a carrier for the carriage of goods is a bailment contract, and also the placing of goods in a warehouse creates the same relation. The custody of an innkeeper of the goods of his guest is one of bailment. From the nature of things it is evident that there can be three general classes of bailments. Arising out of the three general classes of bailments, it is said there are three degrees of negligence classified as follows: In the case of a bailment for the sole benefit of the bailor, such as where one leaves his goods to be cared for by another without compensation, the bailee is required to exercise slight diligence, and he is held liable for gross negligence. Where the bailment is for the sole benefit of the bailee, as in an ordinary case of borrowing, the bailee must exercise a high degree of diligence and is liable for slight negligence; where the bailment is for the benefit of both the bailee and the bailor, as in the case of the watch above mentioned, the bailee is required to exercise ordinary diligence, and is liable for ordinary negligence. It must be apparent that the same actual care and attention required to be exercised in the care of articles varies more because of other circumstances than the mere fact of the agreement as to compensation existing between the owner and the bailee.

[6] Watts v. Boston & Lowell R. R. Co., 106 Mass. 466, (1871).

[7] Van Zile, Bailments and Carriers, § 3.

For instance, the amount of actual care and attention required of one having custody of a load of coal would be entirely insufficient for one having the custody of diamonds, and that, therefore, the duty of diligence resolves itself into the requirement that such care and caution shall be used as is proper under all the circumstances of each particular case. The Supreme Court of the United States has said:

"That the theory that there are three degrees of negligence, described by the terms 'slight', 'ordinary', and 'gross', has been introduced into the common law from the Roman law. It may be doubted if the three terms can be usefully applied in practice. Their meaning is not fixed or capable of being so. One degree thus described not only may be confounded with another, but it is quite impracticable exactly to distinguish them. Their signification necessarily varies according to circumstances to whose influence the courts have been forced to yield. There are so many real exceptions that the rules themselves can scarcely be said to have had a general operation. How much care will, in a given case, relieve a party from the imputation of 'gross negligence', or what omission will amount to the charge, is necessarily a question of fact, depending upon a great variety of circumstances which the law cannot exactly define. Indeed, what is common or ordinary diligence is more a matter of fact than of law. The law furnishes no definition of the term gross negligence or ordinary negligence which can be applied in practice, but it must be left to the jury to determine in each case what the duty is, and what amounts to a breach of it. It would seem that imperfect and confessedly unsuccessful attempts to define that duty had better be abandoned. It may be added that some of the ablest commentators on the Roman law and on the Civil Code of France, have wholly repudiated this theory of three degrees of negligence as unfounded in principles of natural justice, useless in practice, and presenting inextricable embarrassments and difficulties."

And again the Supreme Court said:

"Some of the highest courts of England have come to the conclusion that there is no intelligent distinction between ordinary and gross negligence, and that gross negligence

is ordinary negligence with a vituperative epithet. Confusion has arisen regarding negligence as a positive, instead of a negative word. It is really the absence of such care as it was the duty of the defendant to use. 'Gross' is a word of description and not of definition. 'Gross negligence' is a relative term. It is doubtless to be understood as meaning a greater want of care than is implied by the term ordinary negligence; but after all, under the circumstances it means the absence of the care that was necessary under all the circumstances." [8]

And in all cases negligence means the absence of that degree of care and caution which one should exercise in view of all the circumstances of a particular case, and as applied to railroads it means that degree of caution and care which, with due regard for all other matters, is to be rendered in conducting the business. Among these are the speed which is desirable, the price which the passenger can afford to pay, the necessary cost of different devices and provisions for safety, and the relative risk of injury from different possible causes, and such care and diligence as the passengers or shippers have a right to expect of the carrier under all the circumstances of the particular case.

§ 73. Duty of Carrier to Protect Freight. The carrier is bound to take all possible care of the goods and he is responsible for every injury which he might have prevented by foresight and prudence, and if an accident occurs by act of God, or the public enemy, it is the duty of the carrier to use the most exact diligence to countervail the effects of it. The occurrence of the accident does not relieve him from the responsibilities of a common carrier with respect to the injured goods. He is still bound to the strictest diligence for the preservation of it from the consequences of the accident. In such cases the conduct of the carrier must be governed by the circumstances under which he is acting. In a case where wheat constituting a cargo of a barge, became wet because of an accident caused by the act of God, it was held that it was not the duty of the master of the barge to take the wheat out to shore and

[8] C. M. & St. P. Ry. Co. v. Arms, 91 U. S. 374, (1876).

dry it, because that would have delayed the transportation of the goods of all the other shippers, but that if the wheat could have been dried on the barge while proceeding on its journey it was the duty of the master to do it.[9]

§ 74. Duty to Sell Injured Cargo. Where goods of a perishable quality are in the hands of a carrier and the consignee refuses to accept them, it is the duty of the carrier to sell them. While a carrier has possession of goods he stands for many purposes in the relation of agent of the owner, and if it is necessary to sell the goods to prevent them from being lost it becomes the carrier's duty to do so, for the benefit of the owner, and this is the rule if it becomes impossible from any other cause whatever to deliver the goods according to the direction of the owner, or to return them to the owner.[10]

§ 75. Loss Due to Nature of Freight. Although the carrier insures the arrival of the property at the point of destination against everything but the act of God, and of public enemies, he does not in all cases warrant that it shall arrive in sound condition. The condition in which it shall arrive depends on the nature of the article to be transported. He is relieved from responsibility where fruit perishes by natural decay, or in any case where the inherent defects of the merchandise itself destroy its value. He does not absolutely warrant live stock against the consequences of its own vitality. Vicious and unruly animals may injure or destroy themselves or each other; frightened animals may die of terror, or starve themselves by refusing food, notwithstanding every precaution it is possible to use. For such occurrences the carrier is not answerable; but to be relieved from responsibility for a loss of this description he must provide all suitable means of transportation, and exercise that degree of care which the nature of the property requires. In arrangements and precautions to guard against injuries occasioned by the faults and vices of animals, he is bound to use the highest degree of

[9] Steamboat Lynx v. King, 12 Mo. 272, (1848).

[10] Dudley v. Chicago, Milw. & St. P. Ry. Co., 58 W. Va. 604, (1906).

diligence and care. The carrier for the carriage of live stock is bound to furnish a car that will resist the struggles of the animals, however unruly, and his duty in this respect is not satisfied by furnishing a reasonably strong car. And if in the course of transportation of live stock they become frightened and in danger of being hurt by further transportation, it is the duty of the carrier to remove the stock from the train if that can reasonably be done.[11]

§ 76. Violation of Shipper's Directions. Where goods are shipped by a carrier the law implies a duty to proceed without unnecessary deviation in the usual and customary course.[12] And if there are two routes, one safe and the other hazardous, it is the duty of the carrier in the absence of express directions on the part of the shipper to take the safe route, and if he is directed by the shipper as to which route he shall take, it is his duty to follow such instructions when practicable.[13] And in general it is the duty of a common carrier, in the absence of any special contract to transport the property to the place of destination by the most usual, safe, direct, and expeditious route.[14] And if a carrier receives goods for transportation, agreeing to hold them until a future date or until the happening of an event, and in violation of such agreement forwards them before that time, it will be liable for damages resulting from such wrongful act.[15]

§ 77. Warranty of Fitness of Vehicle. It is the duty of common carriers by water to see that their vessels are seaworthy. In a case where a barge was sunk and a cargo of wheat lost it was said, on the question of seaworthiness:

"That the vessel must be so tight that the water will not reach the cargo, so strong that the ordinary application of external force will not spring a leak or sink her, so sound that she will safely carry the cargo through the ordinary shocks to which she must every day be subjected."

[11] Smith v. New Haven & North Hampton R. R., 12 Allen 531, (1866).
[12] Davis v. Garrett, 6 Bing. 716, (1830).
[13] Express Co. v. Kountze, 88 Wall. 342, (1869).
[14] Merchants Despatch Trans. Co. v. Kahn, 76 Ill. 520, (1875).
[15] Campion v. Canadian Pac. Ry., 43 Fed. Rep. 775, (1890).

If she is capable of this she is seaworthy; if she is not, she is unfit for the navigation of the river. No other test can be given, and this must be determined by the facts in each particular case.[16] The doctrine of warranty of road-worthiness of vehicles has been generally repudiated as applied to carriers by land. They are held liable only for negligence in the selection and maintenance of vehicles.[17]

§ 78. Duty to Deliver to Consignee. Common carriers are bound to deliver as well as to carry goods. In respect to the delivery of goods it will be presumed that a carrier has contracted to carry the goods on the same terms and in the same manner as has been his custom, and if it has been his general custom to deliver goods to houses to which they are directed, and he maintains facilities for that purpose he will be required to deliver goods which he undertakes to carry.[18] For a similar reason if cars are set on private switches or sidings used and owned by factories or warehouses, and the like, if such has been their previous course of business, the carrier's liability as insurer will be brought to an end by such a delivery.[19]

§ 79. Time and Manner of Delivery. The consignee is not bound to accept goods tendered to him after the termination of business hours, and if he refuses to receive goods tendered at such a time it is the duty of the carrier to keep them safely under all his responsibilities, in a store, or under safe custody. Such a delivery will not discharge the carrier from his liability as carrier, and if the goods are destroyed during the night the carrier will be liable for them as such.[20] A carrier by wagon is bound to deliver his freight directly to the consignee. Carriers by railroad and canal usually deliver at warehouses belonging to themselves or others. A carrier by water is presumed to carry from port to port, or wharf to wharf. He is not bound to

[16] Northern Belle, 9 Wall. 526, (1870).

[17] McPadden v. N. Y. C. R. R. Co., 44 N. Y. 478, (1871).

[18] Golden v. Manning, 2 W. Bl. 916, (1773).

[19] East St. L. Connecting Ry. v. Wabash St. L. and Pac. Ry., 123 Ill. 594, (1888).

[20] Hill v. Humphreys, 5 W. & S. 123, (1842).

deliver at the warehouses of the consignees. It is a duty of the consignee to receive the goods out of the ship or on to the wharf, but to constitute a valid delivery on the wharf, the carrier should give due and reasonable notice to the consignee so as to afford a fair opportunity of providing suitable means, or put them in proper care and custody. Such a delivery to be effectual should not only be at the proper place, which is usually the wharf, but at the proper time. If the carrier deposits goods at a wharf at night, or on Sunday, or before the consignee has proper time and opportunity to take them into his possession and care, and abandons them, without a proper custodian, it will not be a fulfillment of his contract to carry and deliver.[21]

§ 80. Proper Place of Delivery. The contract of a common carrier of goods requires him to deliver to the consignee at a suitable place, and the duty to deliver is not discharged by merely bringing the goods to the place designated for delivery. The carrier is bound to unload them with due care, and put them in a place where they will be reasonably safe and free from injury, and until this is done the duty and responsibility of the carrier does not end. It has been held that the duty to deliver at a proper place was not discharged by a railroad company unloading coal on the ground without any protection to keep it from becoming mixed with mud and dirt, and that the company was liable for the damages resulting from such a course, and the responsibility as common carrier of goods remains on the common carrier until delivery is effected, even though the means of effecting the delivery is obtained from the consignee.[22]

§ 81. Express Contract as to Place of Delivery. If a carrier agrees to deliver goods at a particular point or warehouse and does so deliver them, he is exonerated from subsequent loss, though they may never actually come to the possession of the consignee or owner. But if the car-

[21] Richardson v. Goddard, 23 Howard 28, (1859).
[22] Rice v. Boston & Worc. R. R. Co., 98 Mass. 212, (1867).

rier is prevented by any cause from delivering the goods at the precise place agreed upon, it will not be a sufficient carrying out of the contract to deliver near the agreed place, and if they are so left, the carrier assumes every risk attendant upon his noncompliance with the contract, and if the goods are destroyed at such a place it is a destruction in transportation before delivery is made, for which the carrier is absolutely liable, except it be caused by the act of God, or the public enemy.[23]

§ 82. **Delivery to Wrong Person.** Where goods are safely conveyed to the place of destination and the consignee is dead, absent, or refuses to receive them, or is not known, or cannot after reasonable diligence be found, the carrier may be discharged from further liability by placing them in a proper warehouse for and on account of the owner. A carrier must at his peril deliver property to the true owner, and if delivery be made to the wrong person, either by an innocent mistake, or through fraud of another, he will be held liable. In a case that arose in New York State a swindler, using the name *B & Co.*, wrote for the price of some bags to *A*, who was a dealer in bags, and in reply received an answer quoting prices, and the swindler using the name *B & Co.* thereupon ordered a quantity, and whereupon *A* shipped the bags by railway to the general address contained in the letter, and upon the arrival at the point to where they were shipped a man called for the bags and paid the freight on them and took them away. Neither the consignor nor the agent of the railroad company knew of any person or firm by the name of *B & Co.*, and there was in fact no such firm, and the letters written under that name was part of a scheme to defraud the dealer out of his property; the agent of the railroad company did not require any identification of the party to whom the bags were turned over, although it was the usual custom to require identification of strangers. No one knew whether the bags were turned over to the person who wrote the letter containing the order or not. It was held that since

[23] Graff v. Bloomer, 9 Pa. 114, (1848).

the goods were consigned to *B & Co.*, it plainly indicated some person or persons who were known by and doing business under that name, but as there was no such firm and never had been, delivery could not be made to the consignee, and that under such circumstances it was the duty of the carrier to warehouse the goods and keep them for the owner, and that the delivery to the person who called for them was wrongful, and that the railroad company was liable to the owner for value of the goods.[24] The above case seems to place a greater duty on the carrier than on the shipper, and if it could have been shown that the goods were delivered to the person who ordered them, the carrier should have been discharged. And further, in a case where a swindler assuming the name of *A. S.*, and giving a postoffice address at Saratoga Springs, wrote a letter to plaintiff asking for a price list of cigars and the plaintiff replied, sending the price list asked for and thereupon *A. S.*, the swindler, ordered a quantity of cigars, and the plaintiff forwarded the same by a common carrier, and at the same time sent a letter to the swindler at his postoffice address, notifying him that he had forwarded the goods. At that time there was in Saratoga Springs a reputable dealer named *Arthur S.* who was in good credit, and reported good in the mercantile agencies, and the plaintiff supposed that he was dealing with *Arthur S.* The carrier carried the packages to Saratoga Springs, and tendered them to *Arthur S.*, who refused to take them, and he afterwards took them to the shop occupied by *A. S.*, and took receipts signed *A. S.* The swindler's real name was not *A. S.*, but he had assumed that name in his dealings. It was held that this was a valid delivery and discharged the carrier, for the reason that it was not the contract of the carrier that he would ascertain who is the owner of the goods and deliver them to him, but to deliver the goods according to the directions. If a man sells goods to *A* and by mistake consigns them to *B* the carrier's duty is performed if he delivers them to *B*, although the unexpressed intention of the for-

[24] Price v. Oswego & Syracuse R. R. Co., 50 N. Y. 213, (1872).

warder was that they should be delivered to *A*, and that since the carrier delivered the goods to the man who ordered them he discharged his whole duty to the consignor.[25] In a case where defendant was a common carrier engaged in transporting merchandise by teams, and received for transportation thirty barrels of flour consigned to "Edward Klein", and the bill directing the shipment was made out "E. Klein", giving a certain address at the intersection of *Y* and *Z* streets in a city, and Edward Klein was engaged in business in the same city about four squares from the corner of *Y* and *Z* streets, the place to which the flour was directed, and the goods were delivered to "I. Kling", who was engaged in business at the intersection of the streets designated, it was held that the carrier was bound to deliver the goods to the consignee or retain them, and that if he acted on the supposition that the consignor had misdirected the goods he did so at his peril.[26]

§ 83. Gratuitous Carriage. Where common carriers engaged in the transportation of grain had adopted a custom of returning the bags of the consignor without additional charge, the return of the bags was not gratuitous, although designated as "free" in the transactions with the carrier, the compensation for the return of the bags was included in the payment for the carriage of the grain. The company, by establishing such a custom, makes the proposition to all persons that if they will become its customers it will carry their bags both ways, without any other compensation than the freight upon the grain. Persons who become its customers in view of such a custom, do so with that understanding, and the patronage, and the freight paid are the consideration for carrying the bags.[27]

§ 84. Limiting Liability. At common law carriers are responsible for the value of the goods they undertake to carry, but they may limit their responsibility by making a special contract, and this may be done in various ways.

[25] Samuel v. Cheney, 135 Mass. 278, (1883).
[26] McCullough v. McDonald, 91 Ind. 240, (1883).
[27] Pierce v. C. M. & St. P. Ry., 23 Wis. 387, (1868).

The limitation of liability may be effected by giving notice to the public that he will not be accountable for freight of a certain description, but such notice must be brought to the attention of the shipper, or his agents.[28] And if after the shipper has actual knowledge of such notice, he ships goods by such carrier, he will be taken to agree that the goods shall be shipped on the terms contained in the notice.

§ 85. Contract Limiting Liability. When the words of a contract of carriage that limits the liability of the carrier can be given effect without including a release from liability for negligence of the carrier, or his servants, it will not be presumed that such contract was intended to include such a release from negligence. Every presumption is against an intention to contract for immunity for not exercising ordinary diligence in the transaction of any business, and the general rule is that contracts will not be so construed unless expressed in unequivocal terms. In a case where a shipper signed a contract releasing a carrier from liability for loss of the goods from any cause whatsoever, it was held that such did not include a release from liability for negligence.[29] And the operation of such a release will be confined to release of the carrier from liability as insurer. In a case where an express company delivered a receipt for express matter exempting the express company from liability for dangers of railroad transportation, or river navigation, or fire, it was held that the issue and acceptance of such a receipt by the owner was binding and had the force of a valid contract between the parties.[30]

§ 86. Contract for Limiting Time for Making Claim. The responsibility of a common carrier may in general be limited by an express agreement made with his employer at the time the goods are accepted for transportation, provided the limitation be such as the law can recognize as reasonable, and not inconsistent with sound public policy.

[28] Mayhew v. Eames, 3 B. & C. 601, (1825).
[29] Mynard v. Syracuse, Bing. and N. Y. Ry., 71 N. Y. 180, (1877).
[30] Grace v. Adams, 100 Mass. 505, (1868).

But such a special contract cannot relieve the carrier from liability for loss caused by negligence, or misconduct of himself, agents, or employes. A provision in a contract limiting the time when a claim shall be made for loss or damage to freight, if reasonable in length of time is valid, because it does not relieve the carrier from any part of the obligations of a common carrier. The carrier under such a contract is bound to the same diligence, fidelity, and care as he would have been required to exercise if no agreement had been made.[31]

§ 87. Limitation of Amount of Liability. Where a receipt issued by an express company which contained a provision that limited the responsibility of the carrier for loss or damage to the sum of fifty dollars, fixed as the value of the article to be carried, it was held that the shipper by accepting such an instrument declared his assent to its terms and conditions, and that such liquidation of the value of the article was for the advantage of both parties, in that it guarded against controversy or difference of opinion in estimating the damage in case of loss, and was a protection against fraud. The amount of compensation for the transportation of property should have relation to the restricted or limited liability assumed in the agreement to transport the goods, and is to a great degree regulated and fixed by its value, and if a party only pays the price fixed for articles of small value or estimated at a low sum he, himself, bears all risks beyond the value fixed in the contract of shipment.[32] On the other hand, the Supreme Court of Minnesota said in regard to a similar receipt, limiting the value of horses shipped at one hundred dollars per head, that the same reason which forbids that a common carrier should, even by express conduct, be absolved from liability for his own negligence, or that of his agents and servants, stood also in the way of any arbitrary preadjustment of the measure of damages, the effect of which was to furnish partial relief from such liability, it would indeed

[31] Express Co. v. Caldwell, 21 Wall. 264, (1874).
[32] Belger v. Dinsmore, 51 N. Y. 166, (1872).

be absurd to say that the requirement of the law as to such responsibility of the carrier is absolute, and cannot be laid aside even by agreement of the parties, but that one-half or three-fourths of it may be by means of a contract limiting the recovery of damages to one-half or one-fourth of the known value of the property, this would be mere evasion which should not be tolerated. The court directed a large part of its criticism to the form of the contract, and called attention to the fact that it did not require a disclosure of value, but fixed an arbitrary value, and left it to the shipper to question the sufficiency of the value fixed, and indicated that such a contract fair in all respects would be upheld by that court, and said further:

"The right of the carrier to require the disclosure by the consignor of the value of the property presented for transportation, where its value is not apparent, is well known. This is reasonable, both to the end that proper care may be taken of the property while it is in the hands of the carrier and because the proper charges for transportation may often depend largely upon value." [33]

The Supreme Court of the United States, in passing on a provision in such a contract, which fixed the value of the goods, said:

"In general, in the absence of fraud or imposition, a common carrier is answerable for the loss of a package of goods though he is ignorant of its contents and though its contents are ever so valuable, if he does not make a special acceptance. However, he can always guard himself by a special acceptance, or by insisting on being informed of the nature and value of the articles before receiving them. If the shipper is guilty of fraud or imposition by misrepresenting the nature or the value of the articles, he destroys his claim to indemnity because he has attempted to deprive the carrier of the right to be compensated in proportion to the value of the articles and the consequent risk assumed, and what he has done has had a tendency to lessen the vigilance the carrier would have otherwise bestowed. It is plain that there would be no justice in allowing the shipper

[33] Moulton v. St. P., Minn. & Manitoba Ry., 31 Minn. 85, (1883).

to be paid after a loss a large sum for an article, he has induced the carrier to take at a low rate of freight on the assertion that its value is a less sum than claimed. The shipper may be held to his agreement fairly made as to value, even where the loss or injury has occurred through the negligence of the carrier. The limitation as to value has no tendency to exempt from liability for negligence. It does not induce want of care; it exacts from the carrier the measure of care due to the value agreed on. The carrier is bound to respond in that value for negligence. The compensation for carriage is based on that value. The shipper is estopped from saying that the value is greater. There is no violation of public policy; on the contrary, it would be unjust and unreasonable, and would be repugnant to the soundest principles of fair dealing and of the freedom of contracting, if a shipper should be allowed to reap the benefit of the contract if there is no loss, and to repudiate it in case of loss. The distinct ground of our decision is that where a contract limiting the liability of a carrier to an agreed value of the goods carried, signed by the shipper, is fairly made, agreeing on the valuation of the property carried, with the rate of freight based on the condition, that the carrier assumes liability only to the extent of the agreed valuation, even in case of loss or damage by the negligence of the carrier, and the contract will be upheld as a proper and lawful mode of securing a due proportion between the amount for which the carrier may be held responsible and the freight he receives and of protecting himself against extravagance and fanciful valuations." [84]

The Supreme Court of Massachusetts, by substantially the same course of reasoning as that used in the case cited above, upheld such a contract, but added to the reasons offered by the Supreme Court of the United States the statement that:

"Looking at the matter practically, everybody knows that the charges of a carrier must be fixed with reference to all the risks of the carriage, including risk or loss from negligence of servants. In the course of time, such negligence is inevitable, and the business of a carrier could not be carried on unless he includes this risk in his rate of compensation. When the parties in this case made their con-

[84] Hart v. Penn. R. R., 112 U. S. 331, (1884).

tract, it is fair to assume that both had in mind all the usual risks of the carriage."

From this it appears that by the better reason and the weight of authority such contracts are valid and binding. The ancient common law permitted carriers to require shippers to disclose the nature and value of goods offered for shipment and required the charge made for freight to be based on such value.[35]

§ 88. **Strikes.** A carrier is not under the same absolute obligation to carry the goods intrusted to him in the usual time that he is to deliver them ultimately at their destination. In the absence of a special contract there is no absolute duty resting upon a railroad carrier to deliver the goods intrusted to him within what would, under ordinary circumstances, be a reasonable time. Not only storms, and floods, and other natural causes may excuse delay, but the conduct of men also. An incendiary may burn down a bridge, a mob may tear up the tracks or disable the rolling stock, or interpose irresistible force or overpowering intimidation, and the only duty resting upon the carrier, not otherwise in fault, is to use reasonable efforts and due diligence to overcome the obstacles thus interposed and to forward the goods to their destination.[36] In the absence of legal excuses he is answerable for any delay to forward them in the time which is ordinarily required for transportation by the kind of conveyance which he uses, but the failure of employes to do their duty in the line of their employment does not amount to such an excuse.[37] For the delay resulting from the refusal of the employes of a railroad company to do duty, the company is responsible. For delay resulting solely from lawless violence of men not in the employment of the company, the company is not responsible, even though the men whose violence had caused the delay but a short time before had been employed by

[35] Gordon v. Hutchison, 1 W. & S. 285; Gibbon v. Paynton, 4 Burr, 2298, (1769).

[36] Geismer v. L. S. & M. S. R. R. Co., 102 N. Y. 563, (1886).

[37] Blackstock v. N. Y. & Erie R. R. Co., 20 N. Y. 48, (1859).

the company. Where employes suddenly refuse to work and are discharged, and delay results from failure of the carrier to supply their places, such conduct is attributable to the misconduct of the employes in refusing to do their duty, and this misconduct in such cases is considered the proximate cause of the delay, and the company is liable therefor. But if the places of the employes are promptly supplied by other men, and then the new employes are prevented from doing their duty by lawless and irresistible violence, the delay, resulting solely from this cause, is not attributable to the misconduct of persons for whose conduct the carrier is in no way responsible. This results from application of the familiar rule that a master is liable for the acts of his servant.[38]

§ 89. Happenings by the Act of God. The carrier will be excused for non-delivery of freight caused by act of God. This has been defined to be an event which could not happen by the intervention of man, or be prevented by human prudence. It includes extraordinary floods, storms, unusual lightning, sudden tempests, severe frosts, great droughts, earthquakes, sudden deaths, and illnesses and the like.[39] But if by the exercise of diligence such an event can be avoided, it will not excuse the non-delivery of the goods. And for such an event to excuse the carrier it must be the immediate cause of the loss, that it is the remote cause is not sufficient.[40] There is a conflict of authority upon the question whether the failure to transport goods with reasonable diligence is the proximate cause of an ultimate loss, by an accident which in itself was caused by act of God. Those cases that hold that negligent delay in transportation, is not the proximate cause are based on the view, that the carrier could not have reasonably foreseen or anticipated that the goods would be overtaken by such an accident as a natural and probable result of the delay, and for that reason the negligent delay

[38] Pittsburgh, Ft. Wayne & Chicago R. R. Co. v. Hazen, 84 Ill. 36, (1876).
[39] Gleason v. Virginia Midland R. R. Co., 140 U. S. 435.
[40] Merritt v. Earl, 29 N. Y. 115.

was not the proximate cause of the loss, and should be disregarded in determining the liability for such loss. A similar course of reasoning has been resorted to in cases where the loss was due to some cause, such as an accidental fire, not caused by negligence on the part of the carrier and within a valid exception in the bill of lading, and the goods were brought within the peril stipulated against, by the negligent delay of the carrier in transportation. For similar reasons it has been held that a loss of goods by reason of their susceptible nature as by freezing or the like, will not render the carrier liable even after negligent delay in transportation, if such could not have been easily foreseen or anticipated as the natural and probable consequence of such delay. On the other hand it was held by the court of Appeals of New York in a case arising out of a flood which caused the destruction of the goods, that the preceding negligent delay on the part of the carrier in consequence of which the goods were overtaken by a flood, was sufficient ground for holding the carrier liable for the loss. The same court adhered to this view in a case of loss by fire covered by a valid exception in the bill of lading. The Illinois Supreme Court followed the New York rule by holding that negligent delay subjecting goods to loss by the Johnstown flood, rendered the carrier liable, and further that a similar delay rendered the carrier liable for the damages to goods by freezing. It seems on principle that it should not be sufficient for the carrier to say by way of excuse, while a proper and diligent transportation of the goods would have kept the goods free from the peril by which they were lost, prompt shipment might have subjected them to some other peril just as great. The only defense that he should be permitted to make of that kind is that the same loss must have happened if there had not been negligence on his part, but by the better reason and weight of authority that would not be a good defense. Where goods were shipped under an agreement that they should be carried to their destination without change of cars and in violation of this contract, the goods

were unloaded and put in a warehouse for the purpose of transferring them into other cars for shipment to their destination, and while there they were destroyed by fire; it was held that the carriers were liable, although the loss by fire was within a valid exemption from liability contained in the bill of lading.[41]

§ 90. Delivery to True Owner. Where by legal proceedings the true owner of goods has compelled a carrier to deliver to him the goods in process of transportation, such delivery is a complete justification for non-delivery according to the directions of the shipper and the terms of the contract of carriage, and even where the carrier has delivered the property to the true owner, who had a right to possession, on his demand, it is a sufficient defense against the claim of a shipper. If the goods are taken under legal process the carrier must promptly notify the shipper of the seizure, so as to give him the opportunity to defend his title. Where a carrier delivers the property on demand, to one claiming to be the rightful owner, he of course assumes the burden of proving, as against the claim of the shipper, that such person was the rightful owner, and entitled to possession at that time.[42] And even in a case where a railroad company received property for transportation in good faith without knowledge that it was the property of the company and thereafter discovered that the property was its own, it has been held that the company might avail itself of the defense that the property belonged to it with the same force and effect that it could have availed itself of the right of the true owner in the case of a third person.[43] But it has been held in Massachusetts that the taking of property by process of law from a carrier does not bind the shipper, and that the carrier is not relieved from the fulfillment of his contract, or his liability as carrier by the intervention of such act of dispossession, any

[41] Green-Wheeler Shoe Co. v. Chicago, R. I. & Pac. Ry. Co., 130 Ia. 123.

[42] Thomas v. No. Pac. Ex. Co., 73 Minn. 185, (1898); The Idaho, 93 U. S. 575, (1877).

[43] Valentine v. Long Island R. R. Co., 187 N. Y. 121, (1907).

more than he is by destruction by fire or loss from theft, robbery, or unavoidable accident.[44] In event of goods being taken by attachment while they are in transportation in the hands of a carrier, it is the duty of the carrier to use due diligence in notifying the shipper, but he is not bound when the goods are so taken out of his possession to follow them up and be at the trouble and expense of asserting the claim thereto of the party to, or through whom he undertook to carry them.[45] But in a case of transportation by water it is the duty of the master of the vessel upon any interference with his possession, whether by legal proceedings or otherwise, to interpose for the owner's protection and to make immediate assertion of his rights and interests by whatsoever measures are appropriate at the time and place. To that extent the master is bound to take part in legal proceedings and to continue them until, after informing his absent consignee both of the facts and the local law, such owner has a reasonable opportunity to take upon himself the burden of the litigation. Under such circumstances it is the duty of the master to remain by the ship until all hope of recovery is gone.[46]

§ 91. **Improper Packing.** If there be some hidden defect in the packing of the goods and damage results from that cause, it is the default of the owner and the carrier is not responsible. But as to the external protection of the goods, the owner is not required to cover them so as to be safe against the accident of rain, or wind, or fire, or happenings by the act of God. These are dangers, the hazards of which are by law imposed upon the carrier, and they are such that they may in general be easily resisted. The object of packing, in general, is to secure convenience, safety, and despatch in the handling and transportation, and not to prevent injury from such accidental causes as rain happening in the course of transit,

[44] Edwards v. White Line Transit Co., 104 Mass. 159, (1870).
[45] Ohio & Miss. Ry. Co. v. Yohe, 51 Ind. 181, (1875).
[46] The M. M. Chase, 37 Fed. Rep. 708, (1889).

against which the carrier is presumed to have provided. The owner may, if he choose, deliver the goods without any external protection, and if he does, and they are of a nature to be injured by the mere handling and carriage in a careful and proper manner and are so injured, the loss will be his own, but if they are otherwise injured, as by rain or other cause for which the carrier is not excused, the loss will fall upon the carrier.[47] In order to charge common carriers with liability as insurers they must be treated in good faith, and any concealment, artifice, or suppression of the truth that increases the amount of their risk will relieve them of liability.[48]

§ 92. **Negligence of the Shipper.** In general the duty rests upon the carrier to load and unload freight delivered at its stations or warehouses, but if the shipper does the loading the carrier will not be liable for his negligence in discharge of that duty.[49]

§ 93. **Fraud of Shipper.** The carrier has a clear right to know the contents of packages offered for shipment, in order that he may fix his compensation and know his risk. The statement of the shipper as to the character of an article not open to inspection is a representation as to a material fact or of the contract, upon which the carrier may rely. If the value or character of the article actually shipped so varies from the contents of the package as represented, as to materially affect the compensation of the carrier, or the risk, or expense of transportation, the carrier is not liable for the article of greater value received under a misapprehension caused by the shipper's untrue statement, and even a neglect or failure to disclose the real value of a package and the nature of the contents, if there be anything in its form, dimensions, or other outward appearance which is calculated to throw the carrier off his guard, will be conduct amounting to fraud upon him. The intention to impose upon him is not material. It is enough

[47] Klauber v. Am. Ex. Co., 21 Wis. 21, (1866).
[48] Am. Ex. Co. v. Perkins, 42 Ill. 458, (1867).
[49] Penn. Co. v. Kenwood Bridge Co., 170 Ill. 645, (1898).

if such is the practical effect of the conduct of the shipper, as if a box or package, whether designedly or not, is so disguised as to cause it to resemble such a box or package which usually contains articles of little or no value, whereby the carrier misled by such deception, is thrown off his guard and neglects to give to the package the care and attention which he would have given it had he known its actual value.[50]

§ 94. Termination of Carriage. In the case of common carriers who transport their goods by wagon and other vehicles, traversing the common highways and streets, and who, therefore, are able to deliver goods at the houses of consignees, their obligation as carrier does not cease until such delivery is made. But it cannot apply in the case of railroads whose line of movement and point of termination are locally fixed. The nature of the transportation, though on land, is much more like that by sea, in respect to delivery, and from the nature of the case merchandise can only be transported along one line, and delivered at its termination or at some fixed place by its side, at some intermediate point. Another distinguishing feature of transportation by railroad is that a car cannot leave the track or line of rails on which it moves; a freight train moves with rapidity and makes very frequent journeys, and a loaded car while it stands on the track, necessarily prevents other trains from passing or coming to the same place. It is, therefore, essential to the accommodation and convenience of all persons interested that a loaded car on arrival at its destination, should be unloaded, and that all the goods carried on it, to whomsoever they may belong, or whatever may be their destination, should be discharged as soon and as rapidly as it can be done with safety. From this necessary condition of the business, and from the practice of these transportation companies of having platforms on which to place goods from the car, in the first instance, and warehouse accommodations by which they may be hereafter securely stored, the goods of each consignment by them-

[50] Bottum v. Charleston & West. Car. Ry., 72 S. C. 375, (1905).

selves, in accessible places ready to be delivered, and such conditions being known to the forwarders of goods, the Supreme Court of Massachusetts has held that there is an implied contract between the railroad companies and the shippers that such companies will carry the goods safely to the place of destination, and there discharge them on the platform, and then and there deliver them to the consignee or party entitled to receive them, if he is there ready to take them forthwith; or if the consignee is not ready to take them, then to place them securely and keep them safely a reasonable time, ready to be delivered when called for, and, therefore, common carriers are responsible as common carriers until the goods are removed from the cars and placed on the platform; that if, on account of their arrival in the night or at any other time, when by the usage and course of business, the doors of the merchandise depot or warehouse were closed, or for any other cause they cannot then be delivered, or if for any reason the consignee is not there ready to receive them, it is the duty of the company to store them and preserve them safely, under the charge of competent and careful servants ready to be delivered, and to actually deliver them when duly called for by the parties authorized and entitled to receive them; and for the performance of these duties after the goods are delivered from the cars, the company is liable, as warehouseman, or keeper of goods for hire, and it is not required to notify consignees in order to change their liability from that of carrier to that of warehouseman.[51]

The precise requirements which are necessary in order to discharge a carrier by railroad or by water from the extraordinary liability as common carrier, when the goods reach their destination, has been the subject of much controversy, and has given rise to different rules relating thereto in the different jurisdictions. It has been held by some courts that the liability as common carriers of the goods is not terminated until the goods have arrived at the

[51] Norway Plains Co. v. Boston & Maine R. R., 1 Gray 263, (1854).

town of their destination, and the consignee has been notified and had a reasonable opportunity to take them away,[52] and by other courts, that if the consignee is present upon the arrival of the goods, he must take them without unreasonable delay. If he is absent, unknown, or cannot be found, the carrier can then place the goods in its freight house and after keeping them a reasonable time if the consignee does not call for them, his liability as a common carrier ceases. If after the arrival of the goods, the consignee has a reasonable opportunity to remove them and does not, he cannot hold the carrier as insurer.[53] It has been held by the English courts:

"That the contract of the carrier being not only to carry, but also to deliver, it follows that to a certain extent the custody of the goods as carrier must extend beyond, as well as precede the period of their transit from the place of consignment to that of destination. *First,* there is in most instances an interval between the receipt of the goods and their departure. Sometimes it is one of considerable duration. *Second,* there is the time which in most instances must necessarily intervene between their arrival at the place of destination and the delivery to the consignee, unless the latter—which, however, is seldom the case—is on the spot to receive them on their arrival. Where this is not the case some delay, often a delay of some hours, as for instance when goods arrive at night or late on Saturday, or where the train consists of a number of trucks which take time to unload, unavoidably occurs. In these cases while, on the one hand the delay being unavoidable cannot be imputed to the carrier as unreasonable, or give a cause of action to the consignor or consignee, on the other hand, the obligation of the carrier not having been fulfilled by the delivery of the goods, they remain in his hands as carrier, and subject him to all the liabilities which attach to the contract of the carrier."

The case, however, becomes altogether changed when the carrier is ready to deliver, and the delay in the delivery is attributable not to the carrier, but to the consignee of the

[52] Moses v. Boston & Maine R. R., 32 N. H. 523, (1856).
[53] Fenner v. Buffalo & St. L. R. R. Co., 44 N. Y. 505, (1871).

goods. Here again, just as the carrier is entitled to a reasonable time within which to deliver, so the recipient of the goods is entitled to reasonable time to demand and receive delivery. He cannot be expected to be present to receive delivery of the goods which arrived in the night time, or of which the arrival is uncertain, as of goods coming by sea or goods by a train, the time of arrival of which is liable to delay. On the other hand he cannot, for his own convenience or by his own laches, prolong the heavier liability of the carrier beyond a reasonable time. He should know when the goods may be expected to arrive. If he is not otherwise aware of it, it is the business of the consignee to inform him. When once the consignee is in fault by delaying to take the goods in a reasonable time, the obligation of the carrier becomes that of an ordinary bailee, being confined to taking proper care of the goods as a warehouseman. He ceases to be liable in case of accident. What will amount to a reasonable time is sometimes a question of difficulty but as a question of fact, not of law.[54] And it has been held by our Federal Courts that to establish a constructive delivery it is necessary for a claimant to show *first,* that he separated the goods from the general bulk of the cargo; *second,* that he properly designated the goods; *third,* that he gave due notice to the consignee of the time and place of delivery.[55] It appears on principles of justice and fair dealing, that the consignee should have notice and a reasonable opportunity thereafter to take the goods before the carrier should be released from his extraordinary liability as carrier.

§ 95. Connecting Carrier. Where there are several successive carriers who engaged in the transportation of goods from the place of their reception to the place of their destination, the liability of each carrier to forward the goods will commence with the reception of the goods and will continue until they are delivered, according to the usage of the business, to the next carrier in the line of transit,

[54] Chapman v. Great West. Ry. Co., 2 Q. B. D. 278, (1880).
[55] The Titania, 131 Fed. 229, (1904).

and when an intermediate carrier deposits property in his own warehouse at some intermediate place in the course of his own route, or at the end of the route where it is his duty to deliver it to the owner, his duty as carrier is not completed, and he will remain liable as carrier for any loss for which common carriers are ordinarily responsible.[56] And when under such circumstances a carrier receives goods under an agreement to transport them over the whole or any part of his own route and then to forward them to a destination beyond, he acts in the twofold capacity of carrier and forwarder, and as such is bound to transmit with reasonable promptness to the next succeeding carrier the instructions of his principal. If these instructions be without restriction as to the subsequent route, intermediate consignment, or mode of transit of the goods, but are in general terms to forward them to a designated destination, he will have discharged his duty as forwarding agent by accompanying their delivery in good order to the carrier of the next usual route of transit, with the like general instructions in terms sufficiently explicit and unambiguous to inform that carrier of their ultimate destination.[57] And if the next carrier in the line of transportation refuses or neglects to receive them, the first carrier may store the goods, and then the nature of his relation changes, and he is relieved from the stringent responsibility originally instituted, and the liability as warehouseman is substituted.[58]

§ 96. Connecting Carrier's Right to Benefit of Exemptions. If a contract of shipment provides that its stipulations shall inure to the benefits of all the carriers in the line of transportation, then such carriers will be entitled to the benefit of it, but if the contract does not so provide, its provisions apply only to the carrier with whom the contract was directly made, and they leave it to that carrier to select the carrier from the termination of its line to the end of the route. The authorities are substantially agreed

[56] Ladue v. Griffith, 11 N. Y. 364, (1862).
[57] Little Miami R. R. Co. v. Washburn, 20 Ohio State 324, (1872).
[58] Rawson v. Holland, 59 N. Y. 611, (1875).

that in such a case the intermediate carrier cannot successfully claim the benefits of the provisions of the original contract.[59]

§ 97. **Lien.** A carrier of goods consigned to one person under one contract has a lien upon the whole for the lawful freight and charges on every part, and a delivery of part of the goods to the consignee does not discharge or waive that lien upon the remainder of the goods without proof of an intention so to do, and when the consignor delivers goods to one carrier to be carried over his route and then over the route of another carrier, he makes the first carrier his forwarding agent, and the second carrier has a lien not only for his own part of the route, but also for any freight on the goods paid by him to the first carrier.[60]

[59] Ad. Ex. Co. v. Harris, 120 Ind. 73, (1889).
[60] Potts v. N. Y. & N. E. R. R. Co., 131 Mass. 455, (1881).

CHAPTER V

SPECIFIC DUTIES AND LIABILITIES OF CARRIERS OF PASSENGERS

RELATION OF CARRIER AND PASSENGER

§ 98. Existence Commonly Implied from Circumstances. The relation of carrier and passenger is a contractual relation, but the existence of the relation is commonly implied from circumstances. The circumstances must be such as to warrant the implication that the one has offered himself to be carried on a trip about to be made, and that the other has accepted the offer, and has received him to be properly cared for until the trip is begun, and then to be carried over the carrier's route to his destination.[1] The carrier usually holds himself out as ready to receive and carry, and is bound to receive and carry all passengers who offer themselves as such at the place provided for receiving passengers, and who take such passage in the vehicles provided for passengers. If a person goes upon cars provided by a railroad company for the transportation of passengers with the purpose of carriage as a passenger with the consent, express or implied, of the railroad company, he is presumed to be a passenger. Both parties must enter into and be bound by the contract. The passenger may do this by putting himself in care of the railroad company to be transported, and the company does it by expressly or impliedly receiving him and accepting him as a passenger. The acceptance of the passenger need not be direct or express, but there must be something from which it may be implied.[2]

§ 99. When Relationship Begins. In the case of carriers that maintain regular stations for receiving and dis-

[1] Webster v. Fitchburg R. R., 161 Mass. 298, (1894).
[2] Ill. Cent. R. Co. v. O'Keefe, 168 Ill. 115, (1897).

charging passengers the relation of a passenger and carrier begins when the passenger has put himself in charge of the company and has been accepted. Where one had procured her ticket, passed through the turnstiles provided by the railroad company, and there delivered her ticket to the company, and entered upon a platform constructed by the company exclusively for passengers, and was about to enter the company's car when she was injured, it was held that she had become a passenger and the company was liable for its failure to exercise towards her the high degree of care required of carriers of passengers.[3] One who has purchased a ticket on a railroad and has entered the waiting room at a station, not an unreasonable length of time before the passenger train is due, to take her on to the place of her destination, is a passenger, and entitled to protection as such.[4]

§ 100. Purchase of Ticket. The purchase of a ticket or possession of a pass does not create the relation of passenger and carrier. If a ticket holder should present himself as a passenger and should be refused transportation, there would be a liability on the part of the carrier for failure to carry out the contract, but there would be no liability to him as passenger. The liability would be for refusal to accept him as a passenger in pursuance of the contract made when he purchased his ticket. Where one holding a pass jumped on a railroad train after it had left the station, and the doors of its passenger coaches were closed, it was held that he was not a passenger because he had not presented himself at the proper time and place for the reception of passengers, and the mere fact that the conductor and engineer knew that he was riding on the train outside of its regular passenger coaches was not sufficient to create the relation.[5] And likewise, where one having in his possession a ticket, jumped on a train that was so crowded that he was compelled to hang on to the steps and afterwards fell off and

[3] Ill. Cent. Ry. Co. v. Treat, 179 Ill. 576, (1899).
[4] Batton v. So. & No. Ala. R. R. Co., 77 Ala. 591, (1884).
[5] Ill. Cent. Ry. Co. v. O'Keefe, 168 Ill. 115, (1897).

was injured, it was held that he had not been accepted as a passenger because he had not placed himself in the place provided for the accommodation of passengers.[6]

§ 101. Creation of Relation on Vehicles that Stop on Signal. In the case of street car companies and other carriers whose vehicles stop on signal, the relation of passenger and carrier is rarely created by express contract, but it usually appears by implication, from circumstances that show that the passenger has offered himself, and has been accepted by the carrier. In a case where plaintiff held up a finger to the driver of an omnibus and upon his doing so the driver stopped the horses, and the conductor opened the omnibus door, and just as the plaintiff was putting his foot on the step of the omnibus the driver, supposing that the plaintiff was in, started the horses and the plaintiff fell and was hurt, the circumstances were held sufficient to justify the jury in finding that the plaintiff was a passenger.[7] It has been held that the stopping of a street car amounts to an invitation to passengers to get on, and any person taking hold of the car when stopped for that purpose, with the purpose of getting on becomes a passenger. In a case where one signaled a motorman in charge of a street car and went toward the car for the purpose of entering it as a passenger, but before he reached it, and when very near to it, a trolley pole and car sign fell and injured him, it was held that he was not a passenger because he had not yet entered upon the property of the street car company, and that he was yet a traveler on the highway.[8] Where one boarded a street car while it was yet moving slowly between signal posts, and remained standing on the running board, no objection or dissent, either by word or sign having been made on the part of the conductor, such circumstances are held to be sufficient to justify the jury in finding that there had been an offer by the passenger and acceptance by the carrier.[9] But where the plaintiff got

[6] Webster v. Fitchburg R. R., 161 Mass. 298, (1894).
[7] Brien v. Bennett, 8 C. & P. 724, (1839).
[8] Duchemin v. Boston Elev. Ry., 186 Mass. 353, (1904).
[9] Lockwood v. Boston Elev. Ry. Co., 200 Mass. 537, (1909).

on a car while it was moving without the knowledge of the conductor or motorman, and the conductor, as soon as he saw him, refused to accept him as a passenger unless he would get above the lower step where he was standing, and the plaintiff refused, it was held that plaintiff never became a passenger.[10]

§ 102. Passage Obtained by Fraud. If one without the knowledge of any of the employes of a carrier authorized to receive or reject passengers, gets on a train and secretes himself for the purpose of obtaining passage from one place to another without paying his fare, he is not a passenger and if injured can not recover. Neither can one claim to be a passenger who induces the conductor to permit him to ride, by payment of a sum less than the regular fare, or who induces the conductor to permit him to ride without the payment of any fare. And in general, one who goes on a road intending to induce the conductor to violate the rules of the company and disregard his obligations to his employer, is not lawfully on the conveyance, and the company will not be responsible for an injury received by such person.[11] In a case where a railroad company had adopted a rule permitting students under eighteen years of age to ride for half fare, it was held that one who was over that age, but whose age had been misrepresented for the purpose of getting advantage of the reduced rate, was not a passenger.[12]

§ 103. Baggage. When one purchases a ticket and pays the ordinary charge therefor, it is implied that the passenger intends to take with him such things as he will need for his personal use. The fare of the passenger includes compensation for the carriage of his baggage, as to which carriers of passengers are to be regarded as common carriers. There need be no distinct contract for the carriage of the baggage. The baggage must be ordinary baggage, such as a traveler takes with him for his personal

[10] Hogner v. Boston Elev. Ry. Co., 198 Mass. 260, (1908).
[11] Wabash & West. Ry. Co. v. Brooks, 81 Ill. 245.
[12] Fitzmaurice v. N. Y., New Haven & Hart. R. R. Co., 192 Mass. 159, (1906).

comfort, convenience, or pleasure on the journey. In general terms, it may include not only his personal apparel but other conveniences for the journey, such as a passenger usually has with him for his personal accommodation. The baggage must be such as is reasonably necessary for the particular journey that the passenger is, at the time of the employment of the carrier, intending to make. It is implied in the contract that the baggage and passenger shall go in the same train. Baggage forwarded subsequently by the passenger's direction, in the absence of any special agreement with the carrier, or of negligence on his part, is liable like any other article of merchandise to the payment of the usual freight.[13] The term "baggage" includes the wearing apparel of the traveler, a reasonable amount of money for traveling expenses, watches, and jewelry carried on the passenger's person, books for instruction or amusement, and in case of a carpenter, tools for his personal use, and by one going on an expedition for hunting, a gun and fishing tackle.[14] A common carrier of a passenger is responsible for the baggage of a passenger. His duty in this respect is the same as a common carrier of goods and he can only excuse himself for the non-delivery at the destination of the passenger by showing that the loss was caused by the act of God, or a public enemy. His responsibility commences when the baggage is delivered to him or his authorized agent.

Liability for Baggage. The term "baggage" does not include large sums of money or securities, for the reason that the carrier is entitled to reasonable compensation for his services in carrying such baggage. The amount of that compensation must vary, as the amount of risk which he takes is varied and although a carrier of passengers is bound to guard one going in his vehicles from violence, the damages he must pay if he neglects his duty are such as would ordinarily be contemplated by the parties on making their contract, or assuming their relative rights and obli-

[13] Wilson v. Grand Trunk Ry., 56 Me. 60, (1868).
[14] Woods v. Devin, 13 Ill. 746, (1852).

gations. Such a carrier is bound to take the passenger and to carry him, together with his baggage, reasonable in size and weight, and in kind and value of the articles filling it, such as is naturally and usually required by a passenger and reasonable for his personal use and comforts with his station in life, while on the way, or at his place of destination. Should the baggage be lost by the carrier or misdelivered or stolen from him, although it may contain large sums of money or articles of great value or things not distinctly for personal use, the carrier is not liable for them. He has never entered into any special contract to carry and deliver them. He owes no duty in regard to them by reason of his calling that is not fulfilled. The absence of notice to him of the purpose to carry them has prevented him from exacting a reasonable compensation for the carriage; and what is more, from making provision for safety in measure with the increase of the hazard incurred. For the carriage of himself, his watch, his purse, and the like, the passenger does, perhaps, make a contract with the carrier; or so does set in operation the duty of the latter when he buys his ticket or takes his passage; and does demand of the carrier a care and diligence up to the needs of the hazard, and render him liable for such damage as is in the contemplation of the contract or the scope of the duty.[15]

Limitation of Liability for Baggage. A common carrier cannot in general limit his common-law liability by a notice. Where a common carrier issued a receipt or check for baggage which contained a provision limiting the common-law liability of the railroad company, it was said, if a common carrier is to be allowed to limit his liability he must take care that every one who deals with him is fully informed of the limits to which he confines it. Baggage is usually identified by means of a check or token, and such a card does not necessarily impart anything else, and the party receiving it may well suppose that it is a mere check, signifying that he has paid his passage and has delivered his

[15] Weeks v. N. Y., N. H. & H. R. R. R. Co., 72 N. Y. 50, (1878).

baggage to the carrier. As to bills of lading and commercial instruments of like character, it may well be held that persons receiving them are presumed from their uniform character and the nature of the business transacted by means thereof, that they contain the terms by which property is to be carried, but checks for baggage are not of that character.[16]

Delivery of Baggage. When baggage has reached its final destination, the carrier must have it ready for delivery at the usual place of delivery, and keep it there until the owner can in the use of due diligence, call for and receive it, and the owner must call for it within a reasonable time and use diligence in removing it, and if he fails to do so the company should put it in their baggage rooms and keep it for him, and from that time their custody of it is that of warehousemen only. The carrier is discharged from liability as carrier as soon as he has kept it ready for delivery a reasonable time, and it has not been called for. When trains arrive at late hours it is the usual custom to deliver and receive baggage, not only during what is called the business hours of the day, but upon arrival of trains in the night, and at almost any hour of the night. The rule applied to the receipt of freight, that should it arrive at unusual hours of business, so that the consignee does not have an opportunity during the hours of business to see and receive it, the carrier shall retain it until the business hours of the next day, does not apply to baggage, which usually accompanies the traveler and ordinarily is required by him on his arrival.[17]

Liability of Connecting Carriers for Loss of Baggage. There are three general lines of authorities on the subject of the liability for loss of baggage in the case of a through trip by connecting carriers; one holding the initial carrier liable on his contract; another holding the particular intermediate carrier liable that caused the loss, based on the theory that the initial carrier acted as agent for each of

[16] Blossom v. Dodd, 43 N. Y. 264, (1870).

[17] Quimit v. Henshaw, 35 Vermont 605, (1863).

the intermediate carriers, and that, for that reason, no one of the carriers in the line of transportation was liable for the default of the other and, therefore, the one responsible for the loss must be sued; and a third, that the last carrier may be sued because the goods were found in his hands injured, or for his failure to deliver in case of total loss. This last theory seems to be based on convenience merely more than on investigation of the actual rights of the parties. It is given some legal basis from the rule that when a thing is shown to be in one condition, that condition will be presumed to continue until the opposite is shown. The goods were delivered to the initial carrier in good condition as shown by his receipt, and it will be presumed that this condition continued until they appeared in the hands of the last carrier in bad condition. This rule of *prima facie* liability is supported by the weight of an authority.[18]

§ 104. Degree of Care Required of a Carrier of Passengers. Because a passenger's life is necessarily entrusted in a great degree to the care of the carrier who transports him, the law deems it reasonable that the carrier should be bound to exercise the utmost care and diligence in providing against those injuries which human care and foresight can guard against. This rule applies not only to carriers who use steam railroads, but those who use horse railroads, stage coaches, steamboats, electric, and cable cars, sailing vessels, and the like. It applies at all times when and in all places where, the parties are in the relation to each other of passenger and carrier; and it includes attention to all matters which pertain to the business of carrying passengers. It extends to the management of trains of cars, to the structure and care of the track, to the inspection of the safety of bridges, the testing and inspection of the materials in use in such structures. The expression "utmost care and diligence", and "most exact care", and the like, used in describing the care which the carrier owes to a passenger means the utmost care consistent with

[18] Kesler v. N. Y. C. & H. R. R. R. Co., 61 N. Y. 538, (1875); Moore v. N. Y., N. H., & H. R. R. R. Co., 173 Mass. 335, (1899).

the nature of the carrier's undertaking, and with a due regard for all other matters which ought to be considered in conducting the business. Among these are the speed which is desirable, the price which passengers can afford to pay, the necessary cost of different devices and provisions for safety, and the relative risk of injury from different possible causes as applied to every detail, the rule is the same, the degree of care to be used is the highest with reference to each particular, which can be exercised in that particular, with a reasonable regard to the nature of the undertaking, and the requirements of the business in all other particulars. A passenger is bound to obey all reasonable rules and orders of the carrier in reference to the business. The carrier may assume that he will obey, and the carrier owes to him no duty to provide for his safety when acting in disobedience.[19] More actual attention, oversight, and inspection may be required of one train than another, or of one part of a railroad than another, as a bridge may require to be inspected oftener than other parts of the road, but the standard of care remains the same.

§ 105. Care of Passengers. One who is injured while riding on a train consisting of freight cars and a combination car, one part of which is designed for passengers and another part for baggage, and he is injured by such jerking and jolting of the car as is ordinarily incident to a train of this kind, and who is familiar with the nature of the business of such a railroad and the manner of conducting it, cannot maintain an action against such a railroad company for his injuries. The law requires that everything necessary to the security of the passengers, consistent with the business of the carrier and the means of conveyance employed, shall be done by the carrier; that a carrier under such circumstances shall exercise the highest degree of care consistent with the practical operation of such a train. The liability of a company for negligence will to a degree be limited by its capacity and fitness to transport passengers, if such capacity and fitness is known to the passenger

[19] Dodge v. Boston & Bangor Steamship Co., 148 Mass. 207, (1889).

when he elects to be transported on it. A short line road doing business, and running only mixed trains is not required to apply all the delicate checks and guards that are in use, and if one employs such a carrier knowing what its capacity is, he must take it as he finds it. Diligence in all these cases is not the perfection of the ideal railroad, it is the practical adequacy of the actual road for the particular duty it undertakes. A carrier having limited fitness and capacity to transport passengers, and whose primary business is to transport logs, is not held to the standard of perfection of an ideal railroad, but must exercise the highest degree of care practicable under the circumstances. In the case of ordinary railroads affording regular passenger service, soliciting such travel, holding themselves out as able to take care of it, and running through passenger trains of great weight at tremendous speed, commensurate care is the supreme or highest practical care. The standard of care, however, has proper regard to the circumstances, that is to say, in reference to every particular the highest degree of care which can be exercised in that particular, with a reasonable regard to the nature of the undertaking and the requirements of the business in all other respects. It is not accurate to say, as is often said, that certain classes of cases involve a relaxation in the degree of care exacted, or that they constitute exceptions to the general rule requiring supreme care. The degree of care is the same. Certain circumstances are recognized as differentiating the result of its exercise; that is, there are particular situations in which commensurate care does not require of certain carriers the same tracks, equipments, and operation as is expected of main trunk lines, operating exclusively passenger trains. A passenger on a freight or mixed train assumes all risks reasonably and necessarily incident to carriage by the method which he voluntarily chooses.[20]

[20] Campbell v. Duluth & North East R. R., 120 N. W. Rep. 375, (1909); Peniston v. C. St. L. & N. O. R. R., 34 La. Ann. 777, (1882); Gleason v. Virginia & Midland R. R. Co., 140 U. S. 435, (1891); Louisville, New Albany, & Chicago Ry. v. Snyder, 117 Ind. 435, (1888); Ingalls v. Bills, 9 Met. 1, (1845).

§ 106. Duty of Passenger to Exercise Care. It is the duty of a passenger to exercise ordinary care and caution to secure his own safety. A common carrier is not an insurer of the personal safety of a passenger. The duty of the passenger and the duty of the carrier to observe proper care and caution is reciprocal. If an adult passenger unnecessarily exposes himself to danger, obvious to a person of ordinary care and diligence, and is injured in consequence, he cannot recover, and the carrier has a right to assume that the passenger will act with reasonable care and caution, and occupy the position or situation to which he has been directed. If a passenger is injured while occupying a place provided for the accommodation of passengers, nothing further is ordinarily necessary to show due care on his part, but if he has left the place assigned for passengers, he must make it appear that by some ground of necessity or propriety, his being in that position was consistent with the exercise of proper care and caution on his part, and if passengers voluntarily take exposed positions with no occasion therefor caused by the management of the road, except by bare license or by non-interference, or passive permission of the conductor, they take the special risks of that position on themselves. It will not be negligence on the part of a carrier that his agents and employes did not restrain a passenger, by physical force, from unnecessarily exposing himself to danger. In a case where passengers were required to get off of a train and walk around a wreck to a point on the other side, to take another train and continue on their passage, and they were directed by the conductor where to go and during the time they were waiting to get on the train that was to carry them on, one of the passengers went to a position nearer to the wreck than he had been directed to go by the officers of the train, and was injured by an explosion of the wreckage, it was held that in making the transfer on foot, around the wreck, at the direction of the conductor, he was a passenger, but that by reason of his having occupied voluntarily a more dangerous position than where directed by the conductor,

it was held that he could not recover for his injuries.[21]

§ 107. Passengers Who Pay No Fare. The relation of passenger and carrier may exist even though the carriage is gratuitous. In a case where the driver of a horse car beckoned to some girls to get on a street car and they did so, it was held that the driver of the horse car was the agent of the company with powers broad enough to accept gratuitous passengers, and that if in violation of his instructions he permitted persons to ride without paying he was guilty of a breach of duty as a servant, but that the girls who accepted the invitation were passengers.[22] On the other hand, it was held that where a boy nineteen years old was invited on a coal train by the conductor that such act was outside of the scope of such conductor's employment, and that since there were no accommodations for passengers on the train the boy was charged with knowledge that he had no rights as passenger, and since he did not pay any fare the conductor could not by inviting the plaintiff to get upon the train create between him and the defendant the relation of passenger and carrier, and that the agency powers of a freight conductor were totally different from that of a passenger conductor, as to the creation of the relation of passenger and carrier.[23] Persons riding gratuitously under a rule of a street railway permitting its employes to ride free at any time are passengers as well as those who pay their fares, and such an employe returning home in the evening, or going to visit a friend, is not a fellow servant within the rules excusing companies for liability for accidents caused by negligence of fellow servants.[24] But where the portion of track where such an employe is being carried is not open to the public, and the car in which he was riding was a special car in which only the laborers who were working on that job for the railroad company were allowed to ride, and such car serv-

[21] Conroy v. C. St. P. M. & O. R. R., 96 Wis. 243, (1897).
[22] Wilton v. Middlesex R. R., 107 Mass. 108, (1871).
[23] Eaton v. Del., Lack. & West. R. R., 57 N. Y. 382, (1874).
[24] Dickinson v. West End Street Ry., 177 Mass. 365, (1901).

ice was furnished to accommodate the company and the laborers, and no fare was charged, it was held that the relation between such a person and the carrier was that of master and servant, not of carrier and passenger.[25]

§ 108. Limitation of Liability Contained in Free Pass. A carrier who undertakes to carry passengers is required to exercise the greatest possible care and diligence. The same extreme care is required, even though the passenger be carried gratuitously. Having undertaken to carry, the duty arises to carry safely. However, one who accepts a free pass for which he pays nothing, and which contains the conditions that in consideration the holder of such pass, while traveling thereon, assumes all risk of accident which may happen to him while traveling on, or getting on or off trains of the railroad company, cannot be allowed to deny that he made the agreement expressed therein because he did not and was not required to sign it.[26] If a carrier accepts and carries a passenger, no such contract having been made, such passenger may maintain an action for negligence in transporting him, even if he be carried gratuitously. The passenger is in no way bound to accept the gratuity of the carrier. There is no rule of public policy that prevents the carrier from fixing as a condition of the issue of a free pass that it shall not be compelled, in addition to carrying the passenger gratuitously, to be responsible to him in damages for the negligence of its servants. It is well known that with all the care that can be exercised in the selection of servants for the management of the various appliances of a railroad train, accidents will sometimes occur, from momentary carelessness or inattention. It is hardly reasonable that besides the gift of free transportation the carrier should be held responsible for these when he has made it the condition of his gift that he should not be. In holding that the carrier is not liable under these circumstances, is not giving any countenance to the idea that a carrier may contract with the passenger

[25] Kilduff v. Boston Elev. Ry., 195 Mass. 307, (1907).
[26] Jacobus v. St. P. & Chicago Ry. Co., 20 Minn. 125, (1873).

to convey him for a less price on being exonerated from responsibility for the negligence of his servants. In such a case the carrier would still be acting in the public employment exercised by him, and should not escape its responsibilities or limit the obligations which it imposes upon him.

On this subject the Supreme Court of Massachusetts said:

"Where one accepts, purely as a gratuity, a free passage on a railroad train upon the agreement that he will assume all risk of accident which may happen to him while traveling in such train by which he may be injured in his person, no rule of public policy requires us to declare such contract invalid and without binding force." [27]

Where a woman was riding on a free pass containing these stipulations: "The person accepting and using this pass thereby assumes all risk of accident and damage to person and property, whether caused by negligence of the company's agent or otherwise," and was injured by the negligence of the company; and where it was shown that her husband had procured the transportation, and that the wife knew the difference between cards and tickets, because her husband had on that day purchased a ticket for a friend, but that she had never had the pass in her possession, and her attention had not been called to the stipulations, it was held that the passenger was simply given permission to ride in the coaches of the railroad company. Accepting this privilege she was bound to know the conditions thereof, that she could not through the intermediation of an agent obtain a privilege, and then plead she did not know upon what condition it was granted. A carrier is not bound any more than any other owner of property who grants a privilege to hunt the party to whom the privilege is given and see that all the conditions attached to it are made known, and the court said:

"We think it may be fairly held that a person receiving a ticket for free transportation is bound to see and know of the conditions granted and printed thereon, which the

[27] Quimby v. B. & M. R. R. Co., 150 Mass. 365, (1890).

carrier sees fit to lawfully impose. This is an entirely different case from that where a carrier attempts to impose conditions upon a passenger for hire, which must if unusual, be brought to his notice. In these cases of free passes the carrier has a right to impose any conditions it sees fit as to time, trains, baggage, connections, and damages for negligence, and the recipient of such favors ought at least to take the trouble to look on both sides of the paper before he attempts to use them." [28]

§ 109. "Free Pass" Not Gratuitous. The conditions exempting a railroad company from liability for negligence in the carriage of persons on a "free pass" do not apply, if any consideration, or thing of value, or service is rendered in consideration of the issue of the so-called "free pass". Where the plaintiff was an owner of a patented car coupling, and was negotiating with a railroad company for its adoption and use by the company, and in pursuance of a request from the company to go to another city to see the superintendent of the company's car department in relation to the matter, the railroad company offering to pay his expenses, and the plaintiff accepted the offer, and the company issued him a "free pass" that purported to exempt the company from all liability under any circumstances, whether caused by negligence or otherwise, it was held that there was a good and valuable consideration for the issue of the so-called pass, and that, therefore, the company was carrying for hire; that it was not competent for the railroad company as a common carrier to stipulate for immunity from loss caused by the negligence of its employes.[29] And it has also been held that a drover traveling on an alleged free pass, issued to him for the purpose of taking care of his stock, is a passegner for hire even though the card which he uses is called a free pass, and it is referred to in his transactions with the railroad company as a free pass. The payment of the freight on the stock paid for the passage.[30]

[28] Boering v. Chesapeake Beach Ry. Co., 193 U. S. 442, (1904).
[29] Grand Trunk Ry. Co. of Canada v. Ansel Stevens, 95 U. S. 655, (1877).
[30] N. Y. Cent. R. R. v. Lockwood, 84 U. S. 327.

§ 110. Conductor's Instructions to Passenger. It is proper for a passenger to obey the instructions which he receives of the officers of the train, and when they tell a passenger to keep his seat and they will at the proper time transfer him to another car or notify him when he reaches his destination, he has a right to trust implicitly their directions, and if they mislead him the carrier will be liable.[31]

§ 111. Continuance of Relation of Carrier and Passenger. The relation of passenger and carrier continues until the journey is completed, and one does not cease to be a passenger in going to and returning from a hotel to obtain meals. Where a through passenger without objection by the company or its agents, alights from a train at an intermediate station, which is a station for the discharge and reception of passengers, for any reasonable and usual purpose, like that of refreshments, or sending of telegrams, or of exercise by walking up and down the platform, he does not cease to be a passenger when so engaged, and retains the right to the protection accorded to such by law. However, there is a distinction in that regard between a through train carrying through passengers, and a local train stopping at all stations to receive and discharge passengers. As to a through train carrying only through passengers, a passenger who leaves the train without the knowledge, consent, or notification of the company, at an intermediate station at which the train stops only for some purpose in connection with its management and operation, as for the purpose of taking water or coal, and not to receive or discharge passengers, must be deemed to have abandoned his relation as a passenger, and to have taken upon himself for the time being all risks incident to his movements. In the case of a local train, the company is bound to know that passengers may be received and discharged at all stations at which a train may stop for that purpose, and it is required to keep the approaches of the train in safe condition for their egress and ingress, but as to a through train, there being no passengers to discharge and none to

[31] C., N. O. & T. P. Ry. v. Raine, 113 S. W. 495, (1908).

receive, a stopping of the train for some purpose connected with its operation creates no necessity for the exercise of vigilance in the matter of attention to approaches to the train, and the company should not be held guilty of negligence if it fails to do so. But if a passenger leaves a through train with the consent and permission of the company or its agents, it is the duty of the company to exercise the same degree of care as is required with respect to passengers on local trains.[32] Where a carrier undertakes to carry a passenger a long distance upon its line and sells him a ticket upon which he may stop at intermediate stations, the passenger in getting on and off the train at any station where he chooses to stop has the rights of a passenger. But, of course, during the interval between his departure from the station and his return to it to resume the journey he is not a passenger.[33]

§ 112. **Termination of Relation of Carrier and Passenger.** Persons getting off of railroad trains remain passengers, and the company owes them duties as such while going about the station looking after baggage, and the transaction of their business matters with the company connected with the termination of the contract of carriage, and while passing over the platforms, and through railroad stations on their way out of the station.[34] In a case where one purchased his ticket and rode on a train as a passenger, until the train had nearly reached the station which was the end of his journey, and the train was then stopped to await the passing of an express train from another direction, and the station had not been called, and one of the passengers voluntarily left the train for the sole purpose of continuing his home journey on foot, it was held that when he so left his car, he thereby terminated his relation with the railroad company as a passenger, and the company was under no obligation to afford him a safe path on his further progress. If a passenger chooses to abandon

[32] Lemery v. Great Northern Ry., 83 Minn. 47, (1901).

[33] Dodge v. Boston & Bangor Steamship Co., 148 Mass. 207, (1889).

[34] Ormond v. Hayes, 60 Tex. 180, (1883); Keefe v. Boston & Albany R. R., 142 Mass. 251, (1886).

his journey at any point before reaching the place to which he is entitled to be carried, the railroad company ceases to be under any obligation to provide him with means of traveling farther.[35] Where a woman and her husband walked from the train shed to a waiting room of the station, and then proceeded along the central passageway in a direction indicated by a signboard as being towards the street, it was held that since the passenger had left the train, passed from the train shed to the passenger station, and had selected one of the several passageways leading to the street, the relation of passenger and carrier had ended, and the burden of proof of negligence was upon her. A woman was a passenger on one of the regular trains of a railroad, and got off a train at a regular station early in the morning, while it was very dark, and by the aid of the light afforded by the train went inside the station, but when the train left she was in utter darkness. The platform of the station was three feet above the ground, extending around the building and had no railing. Immediately after entering the station the passenger had occasion to seek a water closet and without any negligence on her part fell from the platform to the ground and sustained the injuries complained of. It was held that she still retained her character as passenger.[36]

§ 113. **Termination of Relation of Carrier and Passenger as to Street Cars.** The street is in no sense a passenger station for the safety of which a street railway company is responsible. When a passenger steps from a street car onto the street he becomes a traveler upon the highway, and terminates his relation and rights as a passenger and the street railway company is not responsible to him, as a carrier, for the condition of the street or for his safe passage from the car to the sidewalk. His rights there are those of a traveler upon a highway and not of a passenger.[37]

§ 114. **Lien of Carrier.** A carrier of passengers is re-

[35] Buckley v. Old Colony R. R. Co., 161 Mass. 26, (1894).
[36] C. R. I. & P. R. R. Co. v. Wood, 104 Fed. Rep. 663, (1900).
[37] Creamer v. West End Street Ry. Co., 156 Mass. 320, (1892).

sponsible as a common carrier for the baggage of the passenger; correspondingly, the carrier of passengers has a lien on the baggage that the passenger carries with him for pleasure, but this lien does not extend to the clothing, or other personal conveniences of the passenger in his immediate use or actual possession. A ticket for transportation on a railway between certain stations, which is silent as to the time when or within which it may be used, does not authorize the holder to stop-over at any point between such stations and resume his journey on the next or following train. The contract involved in the sale and purchase of such a ticket is an entire one and not divisible. It is a contract to carry the passenger through to the point of his destination as one continuous service, and not by piece measure to suit his convenience or pleasure. Where one riding on a ticket that did not provide for stop-overs got out of a train at an intermediate station and remained until the next train, it was held that he had no right to demand that he be carried farther on his original ticket, and that the carrier might either eject him or hold a lien on his baggage for his fare for the remainder of the trip.[38]

RELATED EMPLOYMENTS

§ 115. Sleeping Car Companies. Like an ordinary railway company engaged in the transportation of freight and passengers, the sleeping car companies transact their entire business over the various railways. Like innkeepers, their cars on the various lines of road are extensively advertised all over the country, setting forth the accommodations and comforts therefrom, and their rates of charges, and the public are earnestly invited to avail themselves of the advantages and comforts they thus offer. The running of these sleepers has become a business and social necessity. Such companies, like hotel keepers, owe the duty to the public by reason of their relation to the public to treat all persons whose patronage they have solicited with fairness and without unjust discrimination. When there are sleep-

[38] Roberts v. Koehler, 30 Fed. Rep. 94, (1887).

ing berths not engaged, it is the duty of such companies upon the payment or tender of the customary price to furnish them to applicants when properly called for by unobjectionable persons. It is the duty of such companies to use all reasonable and proper means within their power to preserve order and decorum in the sleepers during the journey, and especially during the sleeping hours, and to furnish and keep on hand such supplies and conveniences as are usually found in like sleepers, and are necessary to the health and comfort of the passengers. None of these duties are ever expressly stipulated for by one engaging a sleeping berth, for the reason that the law always implies them from the relation of the parties created by the contract securing the berth.[39] It invites passengers to pay for and make use of the cars for sleeping, all parties knowing that during the greater part of the night the passenger will be sleeping, powerless to protect himself or to guard his property. He cannot, like the guest of an inn, by locking the door, guard against danger. He has no right to take any such steps to protect himself in a sleeping car, but by the necessity of the case is dependent upon the owners and officers of the car to guard him and the property he has with him from danger from thieves or otherwise, while the law raises the duty on the part of the car company to afford him this protection. Sleeping car companies are not liable as common carriers or as innkeepers, yet it is their duty to use reasonable care to guard the passengers from theft, and if, through want of such care, the personal effects of a passenger, such as he might reasonably carry with him, are stolen, the company is liable for it. Such a relation is required by public policy, and by the true interests of both the passenger and the company, and the deciding weight of authority supports it.[40] It has also been held that steamboat owners carrying passengers are not liable as innkeepers; they are liable as common carriers as to the baggage of the passengers; but they are not, like innkeepers,

[39] Nevin v. Pullman Palace Car Co., 106 Ill. 222.

[40] Lewis v. N. Y. Sleeping Car Co., 143 Mass. 267, (1887).

liable for a watch worn by a passenger on his person by day and kept with him for his use at night, whether retained on his person, or placed under his pillow, or in a pocket of his clothing hanging near him, it is not so entrusted to their custody and control as to make them liable for it as common carriers, and they are not in possession of it by implication of law.

PART III

INTERSTATE COMMERCE LAW

CHAPTER I

COMMERCE CLAUSE OF CONSTITUTION

§ 1. Origin and Occasion Of. The beginning of the Federal Constitution may be said to have emanated in large measure from a desire to secure relief from the burdensome and discriminatory regulations imposed upon commerce by the several States under the Confederacy. Each State in the interest of its own commerce and local conditions legislated without regard to the larger commercial interests and rights of the whole country. The result was that commerce between the States was hampered by conflicting and discriminatory laws, and one of the conditions which led to the adoption of the Federal Constitution was the necessity for securing uniformity and harmony in commerce laws. Said Marshall, C. J.:

"It may be doubted whether any of the evils proceeding from the feebleness of the Federal Government, contributed more to that great revolution which introduced the present system, than the deep and general conviction that commerce ought to be regulated by Congress."[1]

Hence, the so-called "Commerce Clause" of the Federal Constitution, providing that Congress shall have power "to regulate commerce with foreign nations, and among the several States, and with the Indian tribes."[2]

The present discussion will be concerned mainly with

[1] Brown v. Maryland, 12 Wheat. 419. [2] Const. U. S., Art. I, § 8, cl. 3.

"commerce among the States", or "interstate commerce", because most of the problems of conflicting State and Federal authority arise out of interstate commerce. It should be borne in mind, however, that while the power to regulate commerce with the Indian tribes, and with foreign nations, is likewise in Congress, the scope of the power is broader than that over interstate commerce. As pointed out by the late Mr. Chief Justice Fuller:

"The power to regnlate commerce with foreign nations and the power to regulate interstate commerce, are to be taken *diverso intuitu,* for the latter was intended to secure equality and freedom in commercial intercourse as between the States, not to permit the creation of impediments to such intercourse; while the former clothed Congress with that power over International commerce, pertaining to a sovereign nation in its intercourse with foreign nations, and subject, generally speaking, to no implied or reserved power in the States. The laws which would be necessary and proper in the one case, would not be necessary or proper in the other."[3]

§ 2. Clause a Grant of Power. The Federal Government, by which is meant the Government of the United States, is a government of limited or enumerated powers. It has only such powers as are given to it by the Federal Constitution. State governments, on the other hand, are governments of unlimited or general powers, except so far as the State Constitution restricts or limits those powers. Unless, therefore, it is restricted by the State or Federal Constitutions, a State may exercise all the powers ordinarily pertaining to a sovereign government. The Federal Government, while supreme and sovereign within its sphere, must find its authority for action in the Federal Constitution. All powers not granted to the Federal Government remain with the States. The powers of the Federal Government include all those expressly granted and those reasonably and necessarily incident thereto. The power over commerce exists by virtue of an express grant in the Constitution, which is quoted in the preceding paragraph.

[3] Champion v. Ames, (Lottery Case), 188 U. S. 321, 373.

§ 3. Relation of Federal and State Governments in Commerce. The Federal power over commerce is supreme within its proper sphere and when exercised excludes State control. This supremacy exists by reason of an express provision in the Federal Constitution which declares that "this constitution and the laws . . . and all treaties made or which shall be made under the authority of the United States, shall be the supreme law of the land."[4] While supreme as regards the several States, this power is not above the Federal Constitution itself, and it must be exercised within the limits prescribed by that instrument. It must, for instance, yield to the Fifth Amendment, if in its exercise it would deprive a person of life, liberty, or property without due process of law, or take private property for public use without due compensation.

Inasmuch as the States retain all powers not conferred upon the Federal Government, the question has been constantly present: What is the proper scope of State action and what is the proper scope of Federal action? This question pertains not merely to the commerce clause but to all parts of the Federal Constitution purporting to define the sphere of the local and the central government. The final decision on all questions of conflict between the two governments is with the Supreme Court of the United States. To the decisions of that tribunal, therefore, one must look in order to ascertain what each government may do with respect to the control of commerce. As will be more fully pointed out in later sections, there were from the beginning two general doctrines of interpretation applicable to the determination of the question involved. The scope of the power of the Federal Government over commerce will depend upon which of these two doctrines be followed. Although the Federal Government has been in existence for more than one hundred years, the entire extent of its jurisdiction over commerce has never been fully determined. While many questions have been settled, new ones—arising out of changed conditions, resulting from the economic and

[4] Const. Art. VI.

industrial development of the country—are continually presenting themselves.

§ 4. Commerce Defined. The word commerce means more than the mere barter and sale of commodities. It is a word of very large import. The term is not defined in the Constitution, and unlike "due process of law", "*habeas corpus*", and other phrases used throughout that instrument, has no accepted juridical or technical meaning. Commerce is not merely commercial intercourse; it is intercourse in all its branches, including navigation and carriage as well as the mere sale and exchange of goods. It includes all the instrumentalities and agencies by which commerce is ordinarily carried on. Accordingly, the New York legislation giving to Livingston and Fulton exclusive right to operate steamboats on the waters within the jurisdiction of the State was held unconstitutional, as an obstruction to commerce between the States, and as an encroachment upon the power of Congress over the subject.[5]

Of equal importance with navigation as intercourse are all other forms of transportation by which commerce is conducted. Transportation is recognized as a constituent part of commerce itself;[6] hence the multitude of railway cases under the commerce clause. Similarly, telegraph and telephone companies are engaged in commerce.[7]

Whether Commercial Purpose Necessary. It has been suggested that a commercial purpose should be the test of the intercourse that is to be considered commerce; yet in Covington Bridge Co. v. Kentucky,[8] the maintenance of a toll-bridge or ferry for persons crossing a river between two States was held to be commerce, although many of those using the bridge or ferry doubtless had no commercial purpose whatsoever. A bridge, said the court, is just as much a vehicle of commerce as is a ferryboat, and the fact that one is movable and the other a fixture makes no differ-

[5] Gibbons v. Ogden, 9 Wheat. 1.
[6] Hopkins v. U. S., 171 U. S. 578.
[7] Pensacola Tel. Co. v. W. U. Tel. Co., 96 U. S. 1.
[8] 154 U. S. 204, 218.

ence in the application of the rule. . . . "The thousands of people who daily pass and repass over this bridge may be as truly said to be engaged in commerce as if they were shipping cargoes of merchandise from New York to Liverpool." As the bridge was between two States, to fix the toll rates thereon was held to be beyond the power of either one of them.

The meaning of the term commerce received elaborate consideration in a recent decision known as the "Lottery Case",[9] holding the carrying from one State to another by independent carriers, of lottery tickets entitling the holder to a certain specified sum of money, to be commerce. But the late Mr. Chief Justice Fuller, expressing therein also the dissent of three other justices, declared:

"When Chief Justice Marshall said that commerce embraced intercourse, he added, commercial intercourse, and this was necessarily so since, as Chief Justice Taney pointed out, if intercourse were a word of larger meaning than the word commerce, it could not be substituted for the word of more limited meaning contained in the Constitution. Is the carriage of lottery tickets from one State to another commercial intercourse?.....If a lottery ticket is not an article of commerce, how can it become so when placed in an envelope or box or other covering, and transported by an express company? To say that the mere carrying of an article which is not an article of commerce in and of itself, nevertheless becomes such the moment it is to be transported from one State to another, is to transform a non-commercial article into a commercial one simply because it is transported. I cannot conceive that any such result can properly follow. It would be to say that everything is an article of commerce the moment it is taken to be transported from place to place, and of interstate commerce if from State to State."

Water has recently been held not to be an article of commerce in the sense of making State legislation prohibiting its diversion from the State unconstitutional.[10] While the commercial element, as strictly understood, may sometimes

[9] 188 U. S. 321, 367, 371.

[10] McCarter v. Hudson County Water Co., 70 N. J. Eq. 695, 65 Atl. 489.

be lacking from the "intercourse" that is the subject of regulation, the element of "intercourse" cannot be dispensed with if the subject of inquiry is to be regarded as "commerce".

Manufacture Is Not Commerce. The element of intercourse in manufacture is lacking. For this reason manufacture and production are not within the commerce clause, and are, therefore, subject to the exclusive control of the States. "Manufacture is transformation—the fashioning of raw material into a change of form for use. The functions of commerce are different. The buying and selling and the transportation incidental thereto, constitute commerce; and the regulation of commerce in the constitutional sense embraces the regulation at least of such transportation."[11] The mere fact that an article is manufactured for exportation and sale outside of the State does not alone make it an article of interstate commerce.[12] Consequently, if a State forbids the manufacture or sale of intoxicating liquors within its borders, one who manufactures only for export cannot claim he is protected by the commerce clause.

Likewise, a combination of manufacturers of sugar within a State is not a violation of the Sherman Anti-Trust law forbidding combinations in restraint of interstate commerce, even though the sugar is made to be sold outside the State. For "commerce succeeds manufacture, and is not a part of it."[13]

In Addyston Pipe Co. v. U. S.,[14] the manufacturers went a step further than mere production, and became transporters and sellers as well. So when by combination they attempted to stifle competition in the selling of cast-iron pipe, their business was held to be commerce, and being interstate commerce as well, was subject to the Federal Sherman Act, enacted pursuant to the commerce clause.

An agreement to bestow labor on articles and return

[11] Kidd v. Pearson, 128 U. S. 1, 20.
[12] Mugler v. Kansas, 123 U. S. 623.
[13] *Per* Fuller, C. J., in U. S. v. E. C. Knight Co., 156 U. S. 1.
[14] 175 U. S. 211.

them is not a transaction of commerce, notwithstanding that the goods may be transported a considerable distance. For instance, a laundry agent in Covington, Kentucky, who calls for soiled clothing in Cincinnati, Ohio, takes it to Kentucky to clean, and then returns it to Ohio, cannot complain against the State occupation tax, for he is not engaged in interstate commerce, and cannot claim the right to be regulated by Congress alone.[15]

Business of Insurance Is Not Commerce. An insurance contract, for equally obvious reasons, is not an instrumentality of commerce. Therefore, insurance companies, whether domestic or foreign, marine, life or fire, are subject to unlimited State regulation, even though insurer and insured are of different States.[16] Said Mr. ~~Chief~~ Justice Field:

"The contracts (of insurance) are not articles of commerce in any proper meaning of the word. They are not subjects of trade and barter offered in the market as something having an existence and value independent of the parties to them. They are not commodities to be shipped or forwarded from one State to another, and then put up for sale. They are like other personal contracts between parties which are completed by their signature and the transfer of the consideration. Such contracts are not interstate transactions, though the parties may be domiciled in different States. The policies do not take effect—are not executed contracts—until delivered by the agent in Virginia. They are, then, local transactions, and are governed by the local law. They do not constitute a part of the commerce between the States any more than a contract for the purchase and sale of goods in Virginia by a citizen of New York whilst in Virginia would constitute a portion of such commerce."[17]

§ 5. Sales the Chief Cause of Commerce. Transportation excepted, almost all the cases involving the commerce

[15] Commonwealth v. Pearl Laundry Co., 105 Ky. 259, 49 S. W. 26; Smith v. Jackson, 103 Tenn. 673, 54 S. W. 981, 47 L. R. A. 416.

[16] Paul v. Virginia, 8 Wall. (U. S.) 168, 19 L. ed. 357; N. Y. Life Ins. Co. v. Cravens, 178 U. S. 389, 44 L. ed. 1116.

[17] Paul v. Virginia, *supra*, footnote 16.

clause, arise out of sales or commercial contracts.[18] It is immaterial for our purpose — namely, an approximate definition of the commerce that is within the "commerce clause"—where the contract of sale in question is made. We have to inquire only whether transportation, interstate or foreign, will result in the performance of the contract. Except in the case of commerce with Indians, to be noticed presently, the completion of the contract must be in a State or jurisdiction different from that of its inception.[19] It is not necessary that the articles sold be shipped separately and directly to each purchaser; the transaction will still be commerce, and interstate or foreign according to the destination, even though the articles be sent to an agent of the seller at this destination.[20] A Pennsylvania agent of a New York house, who receives and delivers goods in Pennsylvania, is engaged in interstate commerce, and is, therefore, not subject to a license tax of the latter State merely because of his soliciting orders there.[21] Likewise, commercial travellers soliciting orders for merchandise, which orders are sent to the wholesale house in another State and goods are shipped pursuant thereto are engaged in interstate commerce. Itinerant peddlers, however, who carry about with them the identical goods sold are not engaged in interstate commerce, even though the goods which they sell were brought into the State by them for sale.[22] Such peddlers are subject to State control within the exercise of its police power, on the theory of necessary prevention of fraud, and for the sake of the public safety.[23]

The scope and limitations of the interstate character of a sale are well illustrated in the recent case of Dozier v. State.[24] An agent for a Chicago photographic concern took

[18] Addyston Pipe Co. v. U. S., 175 U. S. 241.

[19] Cook v. Rome Brick Co., 98 Ala. 409, 12 So. 918.

[20] Caldwell v. N. C., 187 U. S. 622.

[21] Rearick v. Pa., 203 U. S. 507, 27 Sup. Ct. Rep. 159; Robbins v. Shelby County Tax. Dist., 120 U. S. 489, 30 L. ed. 496.

[22] See *infra*, § 23.

[23] See *infra*, § 26. State v. Wheelock, 95 Iowa 577, 30 L. R. A. 429; Brennan v. Titusville, 153 U. S. 289, 38 L. ed. 719.

[24] 218 U. S. 124, 54 L. ed. 965, 28 L. R. A. (N. S.) 264.

orders in Alabama for "crayon enlargements", for which the purchasers agreed to pay a stipulated price. These enlargements, as was contemplated in the order, were sent, already framed, to the agent and by him displayed to the subject, who if his fancy was caught by the additional beauty of the frame, paid an extra price for it, or else took the picture unframed. On the issue as to whether a sale of the frame, under such circumstances, constituted a transaction of interstate commerce, the Supreme Court of the United States decided in the affirmative. Said Mr. Justice Holmes:

"No doubt it is true that the customer was not bound to take the frame unless he saw fit, and that the sale of it took place wholly within the State of Alabama, if a sale was made. But.....commerce among the States is a question depending upon broader considerations than the existence of a technically binding contract, or the time and place where the title passed.....We are of the opinion that the sale of the frames cannot be so separated from the rest of the dealing between the Chicago company and the Alabama purchaser as to sustain the license tax upon it. Under the decisions the statute as applied to this case is a regulation of commerce among the States, and void under the Constitution of the United States."

Almost simultaneously, the Supreme Court of Missouri reached the contrary conclusion, holding "the sale of these frames was a distinct transaction from that of the order and purchase of the portraits," and could be regulated by the State without encroaching upon the power of Congress.[25]

C. O. D. Shipments. C. O. D. shipments, that is, shipments under instructions to the carrier not to deliver the goods without payment therefor, have caused great diversity of opinion among the State courts. Some contend that such shipments are at the risk of the buyer and, therefore, that delivery is completed when the merchandise is given to a carrier for transportation; others, that the sale is not

[25] State of Missouri v. Looney, 29 L. R. A. (N. S.) 412.

completed until the goods are delivered to the consignee at the point of destination. Refusing to nullify the commerce clause as to all the multitude of transactions involving retention of title in the vendor of goods until payment, the Supreme Court of the United States has definitely decided that where merchandise is received by a carrier with instructions to collect the price on delivery to the consignee in another State, the shipment is interstate commerce.[26]

§ 6. Commerce Limited to Legitimate Subjects of Trade. That purchase, sale, and exchange are the principal objects of interstate and foreign commerce is established; it remains to determine what are the proper subjects of such sale, purchase, and exchange. In general, all such articles as may be legally bought and sold.[27] Whatever products have from time immemorial been recognized by custom or law as fit subjects for barter or sale, must be recognized as legitimate articles of commerce.[28] An infected article, such as diseased beef, is not a legitimate subject of trade, and hence is not within the protection of the commerce clause of the Constitution, but may be freely regulated by the police power of the State.[29] In the case of Austin v. Tennessee, the State Supreme Court,[30] in sustaining the Tennessee statute putting the ban on cigarettes, placed its decision partly upon the same ground, namely, that cigarettes are not legitimate articles of commerce.[31] The Supreme Court of the United States, while indicating that in its opinion tobacco was clearly a legitimate article of commerce, and interstate traffic in it was beyond control of the States, avoided determination of this particular issue by deciding the case upon another ground.[32] Similarly, adul-

[26] American Express Co. v. Iowa, 196 U. S. 133; Adams Express Co. v. Com., 87 S. W. 1111.

[27] Leisy v. Hardin, 135 U. S. 100; Schollenberger v. Pa., 171 U. S. 1.

[28] Mr. Justice Brown, in Austin v. Tenn., 179 U. S. 343.

[29] Bowman v. Chicago R. R., 125 U. S. 465, 489.

[30] 101 Tenn. 563.

[31] *Contra*, Iowa v. McGregor, 76 Fed. 956; State v. Goetze, 43 W. Va. 495; Sawrie v. Tenn., 82 Fed. 615.

[32] Austin v. Tenn., 179 U. S. 343; see also *infra*, "Original Package Doctrine."

terated articles are not legitimate articles of commerce; so while oleomargarine might come within the commerce clause, still if it is colored in imitation of genuine butter it is not a lawful subject of commerce, and by State legislation, may be excluded from the markets of the State.[33] But a State cannot, to protect its people from fraud, require oleomargarine to be colored pink before it can be sold as a substitute for butter, since such regulation would practically prohibit the sale of all oleomargarine.[34] The court said:

"In a case like this it is entirely plain that if the State has not the power to absolutely prohibit the sale of an article of commerce like oleomargarine in its pure state, it has no power to provide that such article shall be colored, or rather discolored, by adding a foreign substance to it, in the manner described in the statute. Pink is not the color of oleomargarine in its natural state. The act necessitates and provides for adulteration.....If this provision for coloring the article were a legal condition, a legislature could not be limited to pink in its choice of colors. The legislative fancy or taste would be boundless. It might equally as well provide that it should be colored blue or red or black. Nor do we see that it would be limited to the use of coloring matter. It might, instead of that, provide that the article should only be sold if mixed with some other article which, while not deleterious to health, would nevertheless give out a most offensive smell." [35]

Intoxicating Liquors—Legitimate Articles of Commerce. Interstate and foreign traffic in them may be regulated by Congress.[36] It is observed that the familiar power of Congress to forbid trade in liquors with the Indians, is referable to the paternal relationship of our government to these people, coupled with the express power over commerce with the Indians, previously discussed, rather than to its general control over legitimate articles of trade, barter, and exchange. How Congress has delegated to the States

[33] Plumley v. Mass., 155 U. S. 461, 467.
[34] Collins v. New Hampshire, 171 U. S. 30, 33.
[35] *Idem*, footnote 34.
[36] Leisy v. Hardin, 135 U. S. 100, 10 S. Ct. 681, 34 L. ed., 128.

authority to legislate upon liquors imported from other States, at a certain stage in their interstate transit, will be discussed in a later section. While a State may, in the exercise of its police power, regulate the sale of intoxicants within its borders,[37] it cannot in any way burden interstate traffic in them; it cannot, for instance, require a certificate that liquor imported into its borders is chemically pure.[38] Still less can a State prohibit the importation of intoxicating liquors from other States or foreign countries.[39]

§ 7. **Congressional Definition of Commerce.** While we have tried to find our definition of commerce in the decisions of the courts, it should be observed that it is really Congress, which, by the exclusion and inclusion, has the power to define what are the subjects of commerce. So far as actual definition is concerned, the courts are really limited to power to decide, in extreme cases, that a subject declared by Congress to be commerce, in fact has no relation to commerce. Should Congress attempt to regulate the business of insurance, for example, the courts might declare the regulation unconstitutional, on the ground that on no permissible view could insurance be commerce.[40] Incidentally, however, the courts do have occasion to define commerce. It is their duty to see that Federal legislation operates only on that commerce which is interstate, foreign, or with Indians, and that none of the other provisions of the Constitution are infringed; in so doing it cannot help defining the terms used. If, on the other hand, the subject regulated has any relation to commerce, the courts will feel bound by a Congressional declaration that it comes within the meaning of the term commerce. This was abundantly evidenced by the decision in the Lottery Case, previously referred to.

Foreign Commerce Is Extra-Territorial. When the Constitution speaks of "commerce with foreign nations", it

[37] Mugler v. Kansas, 123 U. S. 623.
[38] Donald v. Scott, 74 Fed. 859; Vance v. W. A. Vandercook, 170 U. S. 438.
[39] Bowman v. Chicago R. R. Co., 125 U. S. 465.
[40] Trade-Mark Cases, 100 U. S. 82.

refers primarily to commerce which in some sense is necessarily connected with such nations, or individuals residing in foreign countries.[41] To Congress, accordingly, and not to any of the States, is power given to regulate such commerce. It is not necessary, to be "foreign", that the commerce considered should consist of buying and selling commodities between citizens of the United States and foreign countries. Navigation which affects foreigners and foreign countries may be foreign commerce. This was well illustrated in the case of Lord v. Steamship Company, involving a Federal statute limiting the liability of owners of vessels for loss of baggage. The question in the case was whether this statute was applicable to a ship plying upon the Pacific Ocean between San Francisco and San Diego, both in the State of California. The Supreme Court held the commerce to be foreign, and legislation by Congress both applicable and proper. The court said:

"The contracts of carriage could not be performed except by going not only out of California, but out of the United States as well.

The Pacific Ocean belongs to no one nation, but is the common property of all. When, therefore, the Ventura went out from San Francisco or San Diego on her several voyages, she entered on a navigation which was necessarily connected with other nations. While on the ocean her national character only was recognized, and she was subject to such laws as the commercial nations of the world had, by usage or otherwise, agreed on for the government of the vehicles of commerce occupying this common property of all mankind. She was navigating among the vessels of other nations and was treated by them as belonging to the country whose flag she carried. True, she was not trading with them, but she was navigating with them, and consequently with them was engaged in commerce. If in her navigation she inflicted a wrong on another country, the United States, and not the State of California, must answer for what was done. In every just sense, therefore, she was, while on the ocean, engaged in commerce with foreign nations, and as such she and the business in which

[41] Veazie v. Moor, 14 How. 568.

she was engaged were subject to the regulating power of Congress. Navigation on the high seas is necessarily national in its character. Such navigation is clearly a matter of 'external concern', affecting the nation as a nation in its external affairs. It must, therefore, be subject of the National Government." [42]

Commerce among the Several States. When the Constitution gave to Congress power to regulate commerce with the several States, it means traffic, intercourse, commercial trading, or the transportation of persons or property between or among the several States, or from or between points in one State and points in another State. Obviously, it is that class of commerce which is the most important, and which gives rise to the most numerous questions of conflicting State and Federal authority. The important test in determining whether commerce is interstate, is whether it crosses a State line. Once having done so, the entire commercial transaction of which it is a part becomes interstate, and as such is within the Federal power conferred by the Constitution upon Congress. Thus the carriage of goods intended for points beyond the State upon a steamer plying on a Michigan river between points wholly in Michigan was sufficient to make that steamer engaged in interstate commerce and subject to the regulation of Congress.

"Whenever a commodity has begun to move as an article of trade from one State to another, commerce in that commodity between the States has commenced. The fact that several different and independent agencies are employed in transporting the commodity, some acting entirely in one State, and some acting through two or more States, does in no respect affect the character of the transaction. To the extent in which each agency acts in that transportation, it is subject to the regulation of Congress." [43]

But carrying a pleasure party on a steamboat is not interstate commerce, even though the boat may touch the shores of different States; the commercial element is lacking; the

[42] Lord v. S. S. Co., 102 U. S. 541, 543.
[43] The Daniel Ball, 10 Wall. 557, 565.

journey is interstate, but there is no commerce.[44] Where the transportation is wholly between points within a State, and is no part of an interstate carriage, it is subject to the regulation only of that State. Even where the carriage, although between points in the same State, goes by a route lying partly in another State, such commerce is, by the weight of State authority, purely internal;[45] but there are some State cases to the contrary.[46] The latter have been upheld by the United States Supreme Court.[47] In that case the question was whether the State Railroad Commission of Arkansas had the right to enforce a State regulation of railroad rates as to a shipment of goods between two points in the State over a line of railroad which for a portion of the distance between those points ran outside of the State. Relying upon a holding of Mr. Justice Field in an early case[48] that "to bring the transportation within the control of the State, as part of its domestic commerce, the subject transported must be within the entire voyage under the exclusive jurisdiction of the State", Mr. Justice Holmes, for the Court, declared that the transportation above referred to was interstate commerce, and as such was subject to Federal regulation and was exempt from regulation by the State. In reply to the argument that the case of Lehigh Valley R. R. Co. v. Pennsylvania had upheld the right of a State to tax the receipts on transportation between two points within the State, when the route is partly over an adjoining State,[49] Mr. Justice Holmes said:

"That case was nevertheless not a denial of the interstate character of transportation; that was the case of

[44] State v. Seagraves, 111 Mo. App. 353, 85 S. W. 925.

[45] Com. v. Lehigh Valley R. R., 17 Atl. Rep. 179; same title, 129 Pa. St. 308; Seawell v. K. C. R. R., 119 Mo. 222, 24 S. W. 1002; Campbell v. Chicago R. R., 86 Iowa 587, 53 N. W. 351, 17 L. R. A. 443.

[46] Burlington R. R. v. Dey, 82 Iowa 312, 48 N. W. 98, 12 L. R. A. 436; State v. Gulf R. R. (Tex. 1898), 44 S. W. 542; Pacific Coast S. S. Co. v. Board of Ry. Commissioners, 9 Sawy. (U. S.) 253, 18 Fed. 10, as to vessels being more than a league from shore.

[47] Hanley v. K. C. So. R. R. Co., 187 U. S. 617, 621, 23 Sup. Ct. Rep. 214.

[48] Pac. Coast S. S. Co. v. R. R. Commissioners, 9 Sawyer 253.

[49] 145 U. S. 192.

a tax and was distinguished expressly from an attempt by a State directly to regulate the transportation while outside its borders. . . . And although it was intimated that, for the purposes before the court, to some extent commerce by transportation might have its character fixed by the relation between the two ends of the transit, the intimation was carefully confined to those purposes. Moreover, the tax 'was determined in respect of receipts for the proportion of the transportation within the State.' . . . Such a proportioned tax had been sustained in the case of commerce admitted to be interstate. . . . Whereas it is decided, as we have said, that when a rate is established, it must be established as a whole."

In a still later case, however, the same justice said:

"It would be an extravagant consequence to draw from the decision denying the right of a State to fix rates over a railway route passing outside its limits, that the Sherman Act would cover a contract, alleged to be in restraint of trade, affecting transportation between two points in the same State, a river forming the boundary between that and another State."[50]

Commerce between States and Territories. The law does not as yet appear well settled as to whether the commerce clause covers commerce between the States and the Territories, or the District of Columbia, as well as commerce between State and State. In Hawley v. Kansas City Southern R. R. Co.,[51] referred to above, the Supreme Court held that it was beyond the power of the State of Arkansas to regulate the rates on goods shipped from a point in Arkansas to another point in the same State, on a through bill of lading, and part of the journey being through the Indian Territory. Mr. Justice Holmes "assumed" that the power of Congress over commerce between a State and Territory was "not less than its power over commerce among the States." This, obviously, is *dictum* merely.

With regard to a decision involving the District of Columbia,[52] the implication from the majority opinion is that such

[50] Cincinnati Packet Co. v. Bay, 200 U. S. 179.

[51] 187 U. S. 617.

[52] Stoutenburgh v. Hennick, 129 U. S. 141, 151.

commerce falls within Federal control. In that case an act of the legislative assembly of the District imposing a license tax on traveling salesmen, was declared to be invalid as a regulation of commerce, upon the ground that Congress could not authorize the District to exercise such power as the subject was one calling for national legislation. The inference is that this power, if exercised at will, should be exercised by Congress itself. In a dissenting opinion, Mr. Justice Miller declared:

"Commerce by a citizen of one State, in order to come within the Constitutional provision, must be commerce with a citizen of another State; and where one of the parties is a citizen of a Territory, or of the District of Columbia, or of any other place out of a State of the Union, it is not commerce among the citizens of the several States."

But as previously indicated, the implication to be drawn from the opinion of the majority of the court is to the contrary.[53]

Commerce with the Indian Tribes. Indian sovereignty is tribal and not territorial. Therefore, the grant of power to regulate commerce with the Indian tribes has been held to include commerce with individual Indians, irrespective of territorial considerations. Thus in United States v. Holliday[54] an indictment for selling liquor to an Indian who at the time was in the State of Minnesota, but not upon a reservation, was sustained under an Act of Congress forbidding the sale of liquors to any Indian under the charge of any Indian agent. Commerce with the Indian tribes was held to mean commerce with the individuals composing those tribes. The court said:

"Is there anything in the fact that this power is to be exercised within the limits of a State, which renders the Act regulating it unconstitutional?.....If commerce, or traffic, or intercourse, is carried on with an Indian tribe, or

[53] U. S. v. Whelpley, 125 Fed. Rep. 616; Beitzell v. D. C. 21 App. Cas. (D. C.) 49.

[54] 3 Wall. 407, 418, 419.

with a member of such tribe, it is subject to be regulated by Congress, although within the limits of a State. The locality of the traffic can have nothing to do with the power. . . . Neither the Constitution of the State nor any act of its legislature, however formal or solemn, whatever rights it may confer on those Indians or withhold from them, can withdraw them from the influence of an Act of Congress which that body has the constitutional right to pass concerning them. Any other doctrine would make the legislation of the State the supreme law of the land, instead of the Constitution of the United States, and the laws and treaties made in pursuance thereof."

This proposition, that Congress may regulate commerce with the Indian tribes, even though such commerce originates and ends within the limits of a single State, is, it should be noted, laid down with regard to commerce with the Indian tribes alone, and is not to be construed as implying that Congress may regulate any other kind of purely internal commerce.

CHAPTER II

CONGRESSIONAL CONTROL AND REGULATION

The control of commerce includes its instrumentalities, chief of which are transportation and communication. Transportation, as is to be expected, furnishes the greatest number of examples of interstate and foreign commerce. Upon the principles previously indicated, it includes transportation of goods and passengers, from one State to another, or from the United States to foreign countries, and every link in that transportation, as well as the means by which the transportation is carried on.[1]

§ 8. **Transportation.** *By Water.* Whether the transportation be by water or by land, the principle is the same. The first and the leading case under the commerce clause, Gibbons v. Ogden,[2] it will be remembered, decided that commerce is intercourse, and that navigation being intercourse, is also commerce. Incident to the transportation of goods by water is that of receiving and landing freight and passengers at a wharf;[3] so is the towing and lightering of vessels in and approaching ports.[4] Ferries across a river or channel separating two States are a means of interstate commerce, and cannot be interfered with by State taxation.[5] Bridges, too, if stretching from State to State, may be themselves means of interstate commerce, and as such, come within the control of Congress by its constitutional power.[6] For similar reasons the "navigable waters of the United States" may be considered means of commerce. How the power to regulate commerce comprehends the control for

[1] Wabash R. R. v. Ill., 118 U. S. 557.

[2] 9 Wheat. 1.

[3] Gloucester Ferry Co. v. Pennsylvania, 114 U. S. 196.

[4] Harman v. Chicago, 147 U. S. 396, 13 S. Ct. 306, 37 L. ed. 216.

[5] St. Louis v. Ferry Co., 11 Wall. 423; Fanning v. Gregoire, 16 How. 524; Wiggins Ferry Co., v. E. St. Louis, 107 U. S. 365.

[6] Pennsylvania v. Wheeling Br. Co., 18 How. 421.

that purpose, and to the extent necessary, of all such navigable waters, will be discussed in a later section.[7]

By Land. Even after Gibbons v. Ogden had decided that transportation by water was commerce, it was said:

"Many of our statesmen entertained doubts as to the existence of the power to establish ways of communication by land. But since, in consequence of the expansion of the country, the multiplication of its products, and the invention of railroads and locomotion by steam, land transportation has so vastly increased, a sounder consideration of the subject has prevailed and led to the conclusion that Congress has plenary power over the whole subject."[8]

The same authority remarks:

"The power to construct, or to authorize individuals or corporations to construct, national highways and bridges from State to State, is essential to the complete control and regulation of interstate commerce. Without authority in Congress to establish and maintain such highways and bridges, it would be without authority to regulate one of the most important adjuncts of commerce. This power in former times was exerted to a very limited extent, the Cumberland or National road being the most notable instance."

So familiar are the countless examples of regulation of railroads and their incidents, that it is deemed unnecessary to cite further instances upon this point. As a very large number of cases under the commerce clause are railway cases, the present proposition will be amply supported by such cases later cited to illustrate other features of this subject.

§ 9. Communication. Next to transportation in importance as a means of commerce, is the communication of intelligence. A telegraph company occupies the same relation to commerce as a carrier of messages, that a railway company does as a carrier of goods.[9] So far as its interstate

[7] See also Gilman v. Phila., 3 Wall. 713, 724.

[8] California v. Central Pac. R. Co., 127 U. S. 1, 39.

[9] Tel. Co. v. Texas, 105 U. S. 460.

and foreign business is concerned, it is subject to the regulating power of Congress; and the power of Congress over the postal service includes also power to authorize and aid in the construction of interstate telegraph lines.[10] The status of the telephone as an instrument of commerce is established by several State cases;[11] and a decision of the Supreme Court by implication recognizes the Federal power over the interstate business of a telephone company, the sole point decided being that a certain statute with regard to telegraph companies could not by inference merely be construed to include telephone companies as well. On principle it would seem that the telephone is equally an instrument of commerce with the telegraph.[12]

The importance of the various means of both transportation and communication, as instrumentalities of commerce, is perhaps nowhere better stated than in the following quotation from Pensacola Tel. Co. v. W. U. Tel. Co.:[13]

"The powers (of Congress) thus granted are not confined to the instrumentalities of commerce, or the postal service known or in use when the Constitution was adopted, but they keep pace with the progress of the country, and adapt themselves to the new developments of time and circumstances. They extend from the horse with its rider to the stage coach, from the sailing vessel to the steamboat, from the coach and the steamboat to the railroad, and from the railroad to the telegraph, as these new agencies are successively brought into use to meet the demands of increasing population and wealth. They were intended for the government of the business to which they relate, at all times and under all circumstances. As they were entrusted to the general government for the good of the Nation, it is not only the right, but the duty, of Congress to see to it that intercourse among the States and the transmission of intelligence are not obstructed or unnecessarily encumbered by State legislation."

[10] Pensacola Tel. Co. v. W. U. Tel. Co., 96 U. S. 1.

[11] Matter of Pa. Tel. Co., 48 N. J. Eq. 91; Muskogee Nat. Tel. Co. v. Hall, 4 Ind. Ter. 18; Cent. Union Tel. Co. v. State, 118 Ind. 194.

[12] Richmond v. So. Bell Telephone Co., 174 U. S. 761.

[13] 96 U. S. 1, 9.

[14] 187 U. S. 137, 147.

§ 10. Incidents of Commerce. In the Trade-Mark Cases[14] it was urged in defense of the original Federal Trade-Mark Act that the trade-mark is a useful and valuable aid or instrument of commerce, and its regulation by virtue of the commerce clause, therefore, belongs to Congress. To this proposition the court answered:

"Every species of property which is the subject of commerce, or which is used or even essential in commerce, is not brought by this clause within the control of Congress. The barrels and casks, the bottles and boxes in which alone certain articles of commerce are kept for safety and by which their contents are transferred from the seller to the buyer, do not thereby become subjects of congressional legislation more than other property. In Paul v. Virginia .....this court held that a policy of insurance made by a corporation of one State on property situated in another, was not an article of commerce, and did not come within the purview of the clause we are considering.....On the other hand, in Almy v. State of California,.....it was held that a stamp duty imposed by the legislature of California on bills of lading for gold and silver transported from any place in that State to another out of the State, was forbidden by the Constitution of the United States, because such instruments being a necessity to the transaction of commerce, the duty was a tax on exports."

The court then proceeded to hold the Trade-Mark Act unconstitutional, not for the reasons indicated above, but because the Act was not confined to foreign, interstate, or Indian commerce, but purported to enact a universal trade-mark system, without regard to whether the trade to which it was to be applied was domestic or otherwise. A later Trade-Mark Act is expressly limited to "trade-marks used in commerce with foreign nations, or with the Indian tribes", but its constitutionality as regulating a mere incident of commerce is yet undecided.[15]

Manufacture, as we have previously seen, is an incident of commerce, but is not commerce. So a packing house

[14] 100 U. S. 82, 95.

[15] Warner v. Searle Co., 191 U. S. 195; Elgin Watch Co. v. Illinois Watch Co., 179 U. S. 665.

is not engaged in interstate commerce,[16] nor is the business transacted on a Stock Exchange within the commerce clause.[17] In the case last cited, the principal facts under consideration were as follows: The members of the Kansas City Live-Stock Exchange acted as commission merchants, selling cattle received at the stockyards to packing houses in Kansas City, Missouri, Kansas City, Kansas, and in other States. The offices of the Exchange were at the stockyards, in a building owned by the stockyards company, located half in the State of Missouri and half in the State of Kansas. The live stock received at the stockyards and sold by the members of the Exchange came from various parts of the United States. A certain rule of the Exchange was attacked as coming within the prohibitions of the Sherman Anti-Trust Law, but this was held not applicable, as the business of the Exchange was not interstate commerce, but was a mere aid or facility to it, affecting interstate commerce, if at all, in but an incidental manner. In this case the court said:

"Many agreements suggest themselves which relate only to facilities furnished commerce, or else touch it only in an indirect way, while possibly enhancing the cost of transacting the business, and which at the same time we would not think of as agreements in restraint of interstate trade or commerce. They are agreements which in their effect operate in furtherance and in aid of commerce by providing for it facilities, conveniences, privileges, or services, but which do not directly relate to charges for its transportation, nor to any other form of interstate commerce. To hold all such agreements void would in our judgment improperly extend the act to matters which are not of an interstate commercial nature.

"It is not difficult to imagine agreements of the character above indicated. For example, cattle, when transported long distances by rail, require rest, food, and water. To give them these accommodations it is necessary to take them from the car and put them in pens or other places for their safe reception. Would an agreement among the land-

[16] U. S. v. Boyer, 85 Fed. 425.

[17] Hopkins v. U. S., 171 U. S. 578, 592, 593, 598.

owners along the line not to lease their lands for less than a certain sum be a contract within the statute as being in restraint of interstate trade or commerce? Would it be such a contract even if the lands, or some of them, were necessary for use in furnishing the cattle with suitable accommodations? Would an agreement between the dealers in corn at some station along the line of the road not to sell it below a certain price be covered by the act, because the cattle must have corn for food? Or would an agreement among the men not to perform the service of watering the cattle for less than a certain compensation come within the restriction of the statute?.....In our opinion all these queries should be answered in the negative.....Is a New Orleans cotton broker who is a member of the Cotton Exchange of that city, and who receives consignments of cotton from different States and sells them on change in New Orleans, and accounts to his consignors for the proceeds of such sales less his commission, engaged in interstate commerce? Is the character of the business altered in either case by the fact that the broker has advanced moneys to the owner of the article and taken a mortgage thereon as his security? We understand we are in these queries assuming substantially the same facts as those which are contained in the case before us, and if these defendants are engaged in interstate commerce because of their services in the sale of cattle which may come from other States, then the same must be said in regard to the members of the other exchanges above referred to."

Where, however, the selling of cattle is not by brokers for others, but directly by the owners, a combination in restraint of trade is clearly within the Sherman Act. Here then is no mere auxiliary incident to commerce under consideration, but commerce itself. In the words of Mr. Justice Holmes,

"When cattle are sent for sale from a place in one State, with the expectation that they will end their transit, after purchase, in another, and when in effect they do so, with only the interruption necessary to find a purchaser at the stockyards, and when this is a typical, constantly recurring course, the current thus existing is a current of commerce among the States, and the purchase of the cattle is a part and incident of such commerce."[18]

[18] Swift & Co. v. U. S., 196 U. S. 375, 398.

§ 11. Nature of Power of Congress. It is expressly to Congress that the Constitution has granted the authority to regulate interstate, foreign, and Indian commerce. Accordingly it may, if it chooses, occupy the whole field of such commerce;[19] but it is to be noted that the Constitution contains, in the commerce clause, no express exclusion of State authority over such commerce. While, therefore, there can be no doubt that the power of Congress is supreme when exercised over interstate commerce, the controversy in judicial decisions has been over the question whether, when this power is not affirmatively exercised by Congress, any room is left for State regulation of commerce—whether, in other words, the power given to Congress is not merely paramount, but is exclusive as well.

Concurrent. In the case of Livingston v. Van Ingen,[20] Chancellor Kent, in holding that certain statutes granting to the plaintiffs the exclusive right of navigating the waters of that State in steamboats were not in violation of the Federal Constitution, said:

"Clearly, then, it is valid, unless the power to make it be taken away by the Constitution of the United States. We are not called upon to say affirmatively what powers have been granted to the general government, or to what extent. Those powers, whether express or implied, may be plenary and sovereign, in reference to the specified objects of them.....But the question here is, not what powers are granted to that government, but what powers are retained by this, and, particularly, whether the States have absolutely parted with their original power of granting such an exclusive privilege, as the one now before us. It does not follow, that because a given power is granted to Congress, the States cannot exercise a similar power..... When the people create a single, entire government, they grant at once all the rights of sovereignty. The powers granted are indefinite, and incapable of enumeration. Everything is granted that is not expressly reserved in the Constitutional Charter, or necessarily retained as inherent in the people. But when a Federal Government is erected

[19] Lottery Cases, 188 U. S. 321; Gilman v. Phila, 3 Wall. 713.
[20] 9 Johns. 507, 574.

with only a portion of the sovereign power, the rule of construction is directly the reverse, and every power is reserved to the members that is not, either in express terms, or by necessary implication, taken away from them, and vested exclusively in the Federal head. This rule has not only been acknowledged by the most intelligent friends to the Constitution, but is plainly declared by the instrument itself. Congress has power to lay and collect taxes, duties, and excises, but as these powers are not given exclusively, the States have a concurrent jurisdiction, and retain the same absolute powers of taxation which they possessed before the adoption of the Constitution, except the power of laying an impost, which is expressly taken away. This very exception proves that, without it, the States would have retained the power of laying an impost; and it further implies, that in cases not excepted, the authority of the States remains unimpaired.

"This principle might be illustrated by other instances of grants of power to Congress with a prohibition to the States from exercising the like powers; but it becomes unnecessary to enlarge upon so plain a proposition, as it is removed beyond all doubt by the Tenth Article of the Amendments to the Constitution. That article declares that 'the powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States, respectively, or to the people'. The ratification of the Constitution by the convention of this State, was made with the explanation and understanding, that 'every power, jurisdiction, and right, which was not clearly delegated to the general government, remained to the people of the several States, or to their respective State governments'. There was a similar provision in the Articles of Confederation, and the principle results from the very nature of the Federal Government, which consists only of a defined portion of the undefined mass of sovereign power originally vested in the several members of the Union. There may be inconveniences, but generally there will be no serious difficulty, and there cannot well be any interruption of the public peace, in the concurrent exercise of those powers. The powers of the two governments are each supreme within their respective constitutional spheres. They may each operate with full effect upon different subjects, or they may, as in the case of taxation, operate upon different parts of the same object. The powers of the two governments cannot indeed be supreme over each other, for

that would involve a contradiction. When those powers, therefore, come directly in contact, as when they are aimed at each other, or at one indivisible object, the power of the State is subordinate, and must yield. The legitimate exercise of the constitutional powers of the general government becomes the supreme law of the land, and the national judiciary is specially charged with the maintenance of that law, and this is the true and efficient power to preserve order, dependence, and harmony in our complicated system of government.....Our safe rule of construction and of action is this, that if any given power was originally vested in this State, if it has not been exclusively ceded to Congress, or if the exercise of it has not been prohibited to the States, we may then go on in the exercise of the power until it comes practically in collision with the actual exercise of some Congressional power. When that happens to be the case, the State authority will so far be controlled, but it will still be good in all those respects in which it does not absolutely contravene the provision of the paramount law."

Exclusive. Quite the opposite doctrine was entertained by Mr. Chief Justice Marshall, who said:

"Previous to the formation of the new Constitution, we were divided into independent States, united for some purposes, but, in most respects, sovereign. These States could exercise almost every legislative power, and, among others, that of passing bankrupt laws. When the American people created a national legislature, with certain enumerated powers, it was neither necessary nor proper to define the powers retained by the States. These powers proceed, not from the people of America, but from the people of the several States; and remain, after the adoption of the Constitution, what they were before, except so far as they may be abridged by that instrument. In some instances, as in making treaties, we find an express prohibition; and this shows the sense of the Convention to have been, that the mere grant of a power to Congress, did not imply a prohibition on the States to exercise the same power. But it has never been supposed, that this concurrent power of legislation extended to every possible case in which its exercise by the States has not been expressly prohibited. The confusion resulting from such a practice would be endless. The principle laid down by the counsel for the plaintiff, in this respect, is undoubtedly correct. Whenever the terms

in which a power is granted to Congress, or the nature of the power, require that it should be exercised exclusively by Congress, the subject is as completely taken from the State legislatures, as if they had been expressly forbidden to act on it."[21]

The grant of power over commerce was held by Mr. Justice Marshall to come within the principle of the foregoing statement. In Gibbons v. Ogden,[22] decided in 1824, Kent's decision upon similar facts was overruled, Marshall, C. J., declaring that the power of Congress over commerce was exclusive and admitted of no State action whatsoever; and that the absence of legislation by Congress was equivalent to an express prohibition on State regulation.

Present Doctrine. From 1824 to 1851 the question whether the power of Congress was exclusive as well as paramount was variously answered in the cases. In 1851 Mr. Justice Curtis, in the leading case of Cooley v. Board of Wardens,[23] said:

"The grant of commercial power to Congress does not contain any terms which expressly exclude the States from exercising an authority over its subject matter. If they are excluded, it must be because the nature of the power, thus granted to Congress, requires that a similar authority should not exist in the States.....The power to regulate commerce, embraces a vast field, containing not only many, but exceedingly various subjects, quite unlike in their nature; some imperatively demanding a single uniform rule, operating equally on the commerce of the United States in every port; and some, like the subject now in question (Local Pilot Regulation), as imperatively demanding that diversity, which alone can meet the local necessities of navigation. Either absolutely to affirm, or deny that the nature of this power requires exclusive legislation by Congress, is to lose sight of the nature of the subjects of this power, and to assert concerning all of them, what is really applicable but to a part. Whatever subjects of this power are in their nature national, or admit only of one uniform system,

[21] Sturges v. Crowninshield, 4 Wheat. 122, 193.
[22] Gibbons v. Ogden, 9 Wheat. 1, 6 L. ed. 23.
[23] 12 How 299, 318, 319, 13 L. ed. 966.

or plan of regulation, may justly be said to be of such a nature as to require exclusive legislation by Congress."

The latter sentence may be said to express the law of today, although the exact application of the doctrine is still unsettled. The question now arising before the court is, What subjects are national in their nature and admit only of one uniform plan of regulation, and what are not, so as to permit State action. If the subject be of the first class then the States are entirely excluded from legislating upon it, even though Congress has not acted, the silence of Congress being equivalent to prohibition of State action. If the subject be of the second class, then the States may regulate it, until Congress acts, when the State regulation will be superseded so far as it is inconsistent with the Federal law.[24] The power of Congress is exclusive in the sense that "no State has power to make any law or regulation which will affect the free and unrestrained intercourse and trade between the States, as Congress has left it, or which will impose any discriminating burden or tax upon the citizens or products of other States coming or brought within its jurisdiction."[25]

Interstate and foreign transportation of persons and property, and the purchase, sale, and exchange of commodities, seem to be the principal subjects requiring the uniformity of regulation which only Congress can apply.[26] The inferential exclusion of State action appears to be stronger in the case of foreign than interstate commerce,[27] and in the case of commerce by water than commerce by land.[28]

§ 12. Federal and State Regulation. As a corollary to the principal proposition, as we shall see later, the States must be conceded the power to legislate on those subjects which can be regulated best by the vary-

[24] Welton v. Mo., 91 U. S. 275, 23 L. ed. 347; W. U. Tel. Co. v. Call Pub. Co., 181 U. S. 92, 21 S. Ct. 561.

[25] Pittsburgh Coal Co. v. Bates, 156 U. S. 577, 588.

[26] Gloucester Ferry Co. v. Pa., 114 U. S. 196; Stoutenburgh v. Hennick, 129 U. S. 141.

[27] Bowman v. Chi. R. R., 125 U. S. 465, 31 L. ed. 700.

[28] Baltimore R. R. v. Md., 21 Wall. 456, 22 L. ed. 678.

ing circumstances of different localities, even though interstate commerce be also indirectly affected; but on these subjects also Congress has power to act, providing the connection with interstate commerce is not too remote, as, for example, it was held to be when Congress attempted to forbid interstate railroads to discharge employes merely because of membership in labor unions.[29] For if Federal legislation affects a subject bearing too remote a relation to commerce, the courts will declare the legislative definition of commerce to be invalid.[30]

Where Congress has regulated commerce, all State laws on the particular subject are at once superseded, so far as they are in conflict with the Federal regulation.[31] These State laws, if otherwise valid—that is, if not regulations of subjects national in character or admitting of only one uniform system of regulation—are, like State bankruptcy laws, merely suspended by the enactment of a superseding Federal statute, and revive on its repeal.[32]

Although Congress has legislated upon a subject, it is possible it may not have covered the whole of it. Despite strong dissent from Mr. Justice Brewer to the effect that Congress once having legislated on a subject, there is no room for such supplementary legislation as a State may deem necessary, Missouri R. R. v. Haber[33] is authority for the proposition that if Congress has left room for valid non-conflicting police laws, a State may enact these despite the presence of Federal legislation upon the same subject. In Reid v. Colorado,[34] a Colorado statute, requiring that, to avoid infection at certain seasons, cattle before being sent into the State should either be kept at some place north of a certain line for ninety days, or that the owner should secure from the State officers a bill of health,

[29] Adair v. U. S., 208 U. S. 161.

[30] See *supra*, § 7, Congressional Definition of Commerce.

[31] Willson v. Black-Bird Creek Marsh Co., 2 Pet. (U. S.) 245; Bowman v. Chi. R. R. Co., 125 U. S. 465.

[32] Henderson v. Spofford, 59 N. Y. 131.

[33] Mo. R. R. v. Haber, 169 U. S. 613; see Prigg v. Com., 16 Pet. U. S. 539.

[34] 187 U. S. 137, 147.

was attacked as conflicting with the Animal Industry Act of Congress.[35] Said Mr. Justice Harlan:

"The difficulty with the defendant's case is that Congress has not by any statute covered the whole subject of the transportation of live stock among the several States, and except in certain particulars not involving the present issue, has left a wide field for the exercise by the States of their power, by appropriate regulations, to protect their domestic animals against contagious, infectious, and communicable diseases."

Similarly, although Congress has forbidden interstate railways to keep signal tower operators on duty more than nine hours in each twenty-four, a recent New York decision upholds a State statute prescribing eight as the maximum hours for such service, even though the particular railroad considered handles both interstate and intrastate traffic.[36] Wisconsin and Texas cases have, however, expressly rejected this doctrine, largely upon the argument that if Congress has fixed nine hours as a working day for a particular interstate occupation, this is a declaration of the Federal policy on the subject, which would be violated by a State statute excluding interstate railroads from the use of their employes on interstate commerce for one of those nine hours. These cases call attention to the fact that the requirement by the State statute of the absence of such an employe during one of those nine hours might be a serious inconvenience and burden upon interstate commerce.[37] Said the New York court:

"There is no conflict; the State has simply supplemented the action of the Federal authorities. It is the same as if Congress had enacted that the classes of employes named might be employed for nine hours or less, and the State had then fixed the lesser number, which was left open by the Federal statute.

[35] Act of May 29, 1884, ch. 60; 1 Fed. Stat. Ann. 451.

[36] People of N. Y. v. Erie R. R. Co., 198 N. Y. 369, 377, 381, 91 N. E. 849, 29 L. R. A. (N. S.) 240.

[37] State v. T. & N. O. R. R., 124 S. W. 984; State v. C. M. & St. P. R. R., 136 Wis. 407, 117 N. W. 686, 19 L. R. A. (N. S.) 326.

"Of course, it is apparent that, if the Federal statute saying that a signal tower operator may not work more than nine hours prevents a State from saying under controlling conditions that he may not work in excess of a lesser number of hours, State legislation of an analogous character on other subjects which readily suggest themselves, such as the proper weight of rails, the safe speed of trains, the necessary proportion of cars to be equipped with air brakes, may be prevented by Federal legislation simply prescribing the minimum rule of precaution, and the protection by the State of the safety of its citizens at least rendered more complicated and difficult; for, unless there shall be in the future such a separation of interstate and local traffic as has not yet occurred, and which might be made extremely burdensome to the railroads, it will seldom happen that agencies employed in moving the former will not also be moving the latter, and, therefore, if the State is prevented by a Federal statute like that before us from adopting additional (but not conflicting) requirements which it deems to be necessary, it will be unable to insure the safety of local passengers and traffic. And it is obvious that a factor of safety like that in the present Federal statute adapted as we must assume to average conditions prevailing throughout the country often will be quite insufficient under the special conditions prevailing in a given state."[38]

Apparently an interesting question is at this writing still open to the decision of the United States Supreme Court.

§ 13. Federal Regulation May Include Prohibition. In the Lottery Case,[39] to which we have had occasion to refer several times, the Federal statute upheld did not merely regulate the carrying of lottery tickets from State to State, but by punishing those who should so carry them, in effect prohibited such carrying. It was argued that in respect of the carrying from one State to another of articles or things that are, in fact, or according to usage in business, the subject of commerce, the authority given to Congress was not to prohibit, but only to regulate. In reply to this argument, the court said, in part:

[38] People of N. Y. v. Erie R. R. *supra.*

[39] Champion v. Ames, 188 U. S. 321, 357; 23 Sup. Ct. Rep. 321.

"In legislating upon the subject of the traffic in lottery tickets, as carried on through interstate commerce, Congress only supplemented the action of those States—perhaps all of them—which, for the protection of the public morals, prohibit the drawing of lotteries, as well as the sale or circulation of lottery tickets, within their respective limits. It said, in effect, that it would not permit the declared policy of the States, which sought to protect their people against the mischiefs of the lottery business, to be overthrown or disregarded by the agency of interstate commerce. We should hesitate long before adjudging that an evil of such appalling character, carried on through interstate commerce, cannot be met and crushed by the only power competent to that end. We say competent to that end, because Congress alone has the power to occupy, by legislation, the whole field of interstate commerce. What was said by this court upon a former occasion may well be repeated here: 'The framers of the Constitution never intended that the legislative power of the nation should find itself incapable of disposing of a subject matter specifically committed to its charge' . . . If the carrying of lottery tickets from one State to another be interstate commerce, and if Congress is of opinion that an effective regulation for the suppression of lotteries, carried on through such commerce, is to make it a criminal offense to cause lottery tickets to be carried from one State to another, we know of no authority in the courts to hold that the means thus devised are not appropriate and necessary to protect the country at large against a species of interstate commerce which, although in general use and somewhat favored in both national and State legislation in the early history of the country, has grown into disrepute and has become offensive to the entire people of the nation. It is a kind of traffic which no one can be entitled to pursue as of right. That regulation may sometimes appropriately assume the form of prohibition is also illustrated by the case of diseased cattle, transported from one State to another. Such cattle may have, notwithstanding their condition, a value in money for some purposes, and yet it cannot be doubted that Congress, under its power to regulate commerce, may either provide for their being inspected before transportation begins, or, in its discretion, may prohibit their being transported from one State to another.....The act of July 2, 1890,[40] known as the Sher-

man Anti-Trust Act, and which is based upon the power of Congress to regulate commerce among the States, is an illustration of the proposition that regulation may take the form of prohibition. The object of that act was to protect trade and commerce against unlawful restraints and monopolies. To accomplish that object Congress declared certain contracts to be illegal. That act, in effect, prohibited the doing of certain things, and its prohibitory clauses have been sustained in several cases as valid under the power of Congress to regulate interstate commerce.....If a State, when considering legislation for the suppression of lotteries within its own limits, may properly take into view the evils that inhere in the raising of money, in that mode, why may not Congress, invested with the power to regulate commerce among the several States, provide that such commerce shall not be polluted by the carrying of lottery tickets from one State to another?"

§ 14. Power of Congress Subject to Constitution. The power of Congress to regulate commerce is complete, but like all others of the Federal government, is subject to the limitations prescribed by the Constitution.[41] If, for instance, in exercising control of commerce, Congress should deem it necessary to take private property either directly, or through the instrumentality of a corporation, it would have to proceed with due regard to the Fifth Amendment, and make just compensation for the property so taken. Again, Congress could hardly prohibit the transportation of cotton or coal or some other legitimate article of commerce from State to State; that would be taking property without due process of law. Yet the power to regulate commerce has, in various examples of the exercise of the power, as shown in the quotation from the Lottery Case given above, amounted to power to prohibit as well, and still been held not to be a taking of property without due process of law. This is further evidenced in the statutes punishing the carrying of obscene matter through the mails.

[40] 26 Stat. 209, ch. 647.

[41] Gibbons v. Ogden, 9 Wheat. 1, 196; Brown v. Maryland, 12 Wheat. 419; Monongahela Nav. Co. v. U. S., 148 U. S. 312.

Therefore, although it has been said that the police power is not by the Constitution delegated to Congress, and under Article X of the Amendments, may be regarded as reserved to the States, respectively, or to the people,[42] it is evident from these examples that there is a power in Congress at least similar or analogous to that exercised by the States as a police power. In the case of Butterfield v. Stranahan,[43] a Federal statute forbidding the "importation into the United States of impure and unwholesome tea", was held, from considerations of public policy, within the power to regulate commerce with foreign nations, and as no violation of the "due process" clause of the Constitution.

§ 15. Delegation by Congress of Power to Regulate. While Congress cannot delegate to a State or municipality its constitutional power to regulate commerce, nevertheless, in cases where the subject of contemplated regulation is not one demanding uniformity of regulation, and one which, therefore, the States may regulate in the absence of Congressional regulation, Congress may declare that such subject shall be regulated by such laws as the States may respectively enact for that purpose.[44]

After the decision in Leisy v. Hardin, to the effect that the prohibition policy of one State cannot be enforced at the expense of interstate traffic in a legitimate article of commerce, and that the right to import intoxicating liquors from one State into another includes by necessary implication the right to sell in the original package, Congress, as previously noted, passed the Wilson Act, subjecting intoxicating liquors shipped into a State to the operation of the police laws of the State immediately upon their arrival, by providing:

"That all fermented, distilled, or other intoxicating liquors or liquids transported into any State or Territory

[42] Justice Brewer in Austin v. Tenn., 179 U. S. 343.

[43] 192 U. S. 470.

[44] Cooley v. Board of Wardens, 12 How. 299; Rhodes v. Iowa, 170 U. S. 412.

or remaining therein for use, consumption, sale, or storage therein, shall, upon arrival in such State or Territory, be subject to the operation and effect of the laws of such State or Territory, enacted in the exercise of its police powers, to the same extent and in the same manner as though such liquids or liquors had been produced in such State or Territory, and shall not be exempt therefrom by reason of being introduced therein in original packages or otherwise."[45]

The Act was attacked both as an attempted delegation of the power to regulate commerce, and as a Federal police law. But the Supreme Court held that Congress had power to decide what matters of commerce do not require national regulation, and to divest them of their interstate character at an earlier period of time.[46] A similar statute has been enacted with regard to imitation dairy products, and also the protection of fish and game.[47] This does not mean, however, that the States may apply their laws while the liquor is still in transit from another State, nor may a State prohibit the importation of liquor for the use of the importer himself,[48] but a State may forbid agents of non-resident liquor dealers from soliciting in the State[49] orders for the purchase of liquor, although such orders may only contemplate a contract resulting from final acceptance in another State.

If Congress were to become convinced that intoxicating liquors were no longer a legitimate article of commerce, and were freighted with injury to public morals, health, or safety, it could probably absolutely prohibit interstate traffic therein; but from the decision of Rhodes v. Iowa, *supra,* it is to be doubted whether Congress could authorize the

[45] Act August 8, 1890, 26 Stat. 313, ch. 728.

[46] *In re* Rahrer, 140 U. S. 545.

[47] Act of May 9, 1902, ch. 784, § 1; Act of May 25, 1900, ch. 533, § 5.

[48] Rhodes v. Iowa, 170 U. S. 412; Vance v. W. A. Vandercook Co., 170 U. S. 438; American Express Co. v. Iowa, 196 U. S. 133; Adams Express Co. v. Iowa, 196 U. S. 147. For example of valid State legislation under Wilson Act, see Pabst Brewing Co. v. Crenshaw, 198 U. S. 17.

[49] Delamater v. S. D., 205 U. S. 93, 27 S. Ct. 447, 51 L. ed. 724; Compare State v. Hickox, 64 Kan. 650, *In re* Bergen, 115 Fed. 339.

various States to withdraw the privilege of importing liquors therein. As the latter situation would necessarily affect the traffic of more than one State, it would seem to be beyond State interference, even under authority of Congress.

§ 16. **Examples of Federal Commercial Legislation.** Before citing suggestive examples of Federal commercial legislation, it may be well to again summarize the extent of the Federal power, this time in the language of the Northern Securities Case:[50]

"By the express words of the Constitution, Congress has power to 'regulate commerce with foreign nations and among the several States, and with the Indian tribes'. In view of the numerous decisions of this court there ought not, at this day, to be any doubt as to the general scope of such power. In some circumstances regulation may properly take the form and have the effect of prohibition..... Again and again this court has reaffirmed the doctrine announced in the great judgment rendered by Chief Justice Marshall for the court in Gibbons v. Ogden, that the power of Congress to regulate commerce among the States and with foreign nations is the power 'to prescribe the rule by which commerce is to be governed'; that such power 'is complete in itself, may be exercised to its utmost extent, and acknowledges no limitations other than are prescribed in the Constitution'; that 'if, as has always been understood, the sovereignty of Congress, though limited to specified objects, is plenary as to those objects, the power over commerce with foreign nations and among the several States, is vested in Congress as absolutely as it would be in a single government having in its constitution the same restrictions on the exercise of the power as are found in the Constitution of the United States'; that a sound construction of the Constitution allows to Congress a large discretion, 'with respect to the means by which the powers it confers are to be carried into execution, which enable that body to perform the high duties assigned to it, in the manner most beneficial to the people'; and that if the end to be accomplished is within the scope of the Constitution, 'all means which are appropriate, which are plainly adapted to that end and which are not prohibited, are constitutional'.

[50] Northern Securities Co. v. U. S., 193 U. S. 197, 335.

In Cohens v. Virginia,[51] this court said that the United States were for many important purposes 'a single nation', and that 'in all commercial regulations we are one and the same people'; and it has since frequently declared that commerce among the several States was a unit, and subject to national control. Previously, in McCulloch v. Maryland, the court had said that the government ordained and established by the Constitution was, within the limits of the powers granted to it, 'the government of all; its powers are delegated by all; it represents all, and acts for all', and was 'supreme within its sphere of action'. As late as the case of *In re* Debs,[52] this court, every member of it concurring, said: 'The entire strength of the nation may be used to enforce in any part of the land the full and free exercise of all national powers and the security of all rights intrusted by the Constitution to its care. The strong arm of the National Government may be put forth to brush away all obstructions to the freedom of interstate commerce or the transportation of the mails. If the emergency arises, the army of the nation, and all its militia, are at the service of the nation to compel obedience to its laws.' ''

Examples of Congressional legislation, therefore, may be looked for with respect to all the subjects of foreign and interstate commerce, the persons engaged in it, and the instruments by which it is carried on.[53] Nor are the examples all of legislation affecting subjects necessarily of a national character and, therefore, exclusively within the control of Congress, but they also include matters of a character merely local in their operation, and upon which the States may legislate in the absence of any legislation by Congress.[54]

With regard to the instrumentalities of commerce, Congress may authorize the construction of roads, highways, and railways that are interstate;[55] may regulate railway rates throughout the United States;[56] can, as evidenced

[51] 6 Wheat. 264, 413.

[52] 158 U. S. 564, 582.

[53] Sherlock v. Alling, 93 U. S. 99.

[54] Crandall v. Nevada, 6 Wall. 35.

[55] Luxton v. North River Bridge Co., 153 U. S. 525; Cal. v Cent. Pac. R. R., 127 U. S. 1.

[56] Hanley v. K. C. So. R. R., 187 U. S. 617.

by the Northern Securities Case, forbid the formation of one corporation to own stock of two competing interstate railways.[57] Similarly, the other instruments and agencies of transportation, such as lighthouses, pilots, rivers and harbors, railroads and telegraph lines, are all under the control of Congress if it cares to exercise it. Congress may, therefore, enact laws providing for the better security of the lives of interstate passengers, as by imposing penalties for failure to have boilers inspected or to provide life-preservers on ships engaged in interstate commerce.[58] Properly confining the regulation to interstate commerce, Congress may also regulate the liability of interstate railroads to their employes.[59] Navigation may be similarly regulated by the establishment of buoys and beacons;[60] by the establishment of a uniform lien in favor of materialmen who supply vessels of the United States;[61] by requiring the enrollment and licensing of vessels engaged in commerce;[62] by controlling, for the purposes of navigation, the navigable waters of the United States, and the lands under them.[63]

Contracts for the purchase, sale, and transportation of specific articles from State to State are also proper subjects for the regulation of Congress. Nor does the fact that the Constitution guaranties the liberty of private contract prevent the exercise of the power.[64] Congress may, therefore, pass such legislation affecting interstate commerce as to secure equal rights to all engaged therein,[65] such as anti-trust laws, forbidding combinations in restraint of

[57] Northern Securities Co. v. U. S., 193 U. S. 197.

[58] The Steam Propeller Thomas Swan, 6 Ben. 42, 23 Fed. Cas. No. 13, 931.

[59] Howard v. Ills. Central, 207 U. S. 463, 28 S. Ct. 141; Watson v. R. R., 169 Fed. 942.

[60] Mobile County v. Kimball, 102 U. S. 691.

[61] The Lottawanna, 21 Wall. 558.

[62] Wiggins Ferry Co. v. E. St. Louis, 107 U. S. 365.

[63] The Steam Propeller Thomas Swan, 23 Fed. Cas. No. 13,931, Cooley v. Board of Wardens, 12 How. 299.

[64] Addyston Pipe Co. v. U. S., 175 U. S. 211.

[65] R. R. Co. v. U. S., 212 U. S. 481, 29 S. Ct. 304; Express Co. v. U. S., 212 U. S. 522, 29 S. Ct. 315.

interstate trade, of which, of course, the Sherman Act is the most familiar example.[66] As indicated in a previous section, however, combinations to control manufacture alone cannot be reached under this power, for manufacture is not commerce.[67] On the other hand, Congress may legislate to prohibit combinations of employes to boycott interstate goods, for trade is the thing affected, rather than mere production.[68] In short, Congress may adopt any appropriate means to protect commerce, even to granting a Federal corporate franchise;[69] and, of course, corporations are as much subject to the control of Congress as are individuals.[70]

Equally within the appropriate means to protect commerce is Federal legislation punishing not merely offenses committed on the high seas, below the grade of piracy and felony (which are expressly provided for in the Constitution)[71] but also any offense interfering with, obstructing, or preventing commerce within the commerce clause, though committed inland, and within the limits of a State, such as counterfeiting within the United States the notes of foreign banks or corporations.[72]

[66] Addyston Pipe Co. v. U. S., *supra.*

[67] U. S. v. E. C. Knight Co., 156 U. S. 1.

[68] Loewe v. Lawlor, 208 U. S. 274; Adair v. U. S., 208 U. S. 161.

[69] Cal. v. Cent. Pac. R. R., 127 U. S. 1; Luxton v. North River Bridge Co., 153 U. S. 525.

[70] Paul v. Virginia, 8 Wall. 168; Gloucester Ferry Co. v. Pa., 114 U. S. 196.

[71] U. S. v. Coombs, 12 Pet. 72.

[72] U. S. v. Arjona, 120 U. S. 479.

CHAPTER III

STATE CONTROL AND REGULATION

A State has the exclusive power to regulate its own internal commerce; but it cannot regulate interstate or foreign commerce except by such laws as only incidentally affect interstate commerce and do not conflict with any act of Congress on the subject. That its purely internal or domestic commerce is under the full and exclusive control of a State, is a proposition requiring no discussion after our examination of the source, scope, and nature of the power of Congress.[1] With such commerce, such as does not affect other nations or States or the Indian tribes, Congress has nothing to do.[2] When, however, a State intentionally or otherwise, imposes a direct burden upon interstate commerce, as by making payment of a license tax a condition precedent to engaging in the same, it encroaches upon the exclusive power of Congress previously defined.[3]

§ 17. Construction of State Statutes. What a particular State statute means as affecting interstate commerce—whether it is intended to be confined to mere internal commerce, for instance—is a matter for the determination of the court of that State, and its construction will ordinarily be accepted as conclusive.[4] But when a statute is attacked as a roundabout means to invade the domain of Federal authority, the Supreme Court of the United States will look into its actual operation and effect, despite the construction placed upon it by the State court.[5] An express

[1] Addyston Pipe Co. v. U. S., 175 U. S. 211.

[2] Lord v. Steamship Co., 102 U. S. 541.

[3] Hall v. DeCuir, 95 U. S. 485; McNeill v. So. R. R. Co., 202 U. S. 543, 26 Sup. Ct. Rep. 722, 50 L. ed. 1142.

[4] Waters-Pierce Oil Co. v. Texas, 177 U. S. 28; C. & O. R. R. v. Ky. 179 U. S. 388.

[5] Morgan's S. S. Co. v. La. Board of Health, 118 U. S. 455.

declaration that a statute is passed in pursuance of the police power of the State and as a police measure, will not be binding upon the Federal courts if the act in fact trenches on that which is within the exclusive power of Congress.[6] After the State court has construed the statute, the Federal question remaining is whether the statute as so construed is valid. It is when the construction of the statute enters into the question of its relationship to the commerce clause, that the construction placed by the State court is not binding upon the Federal court. In 1895 the State of South Carolina passed a liquor dispensary law which was intended as a *bona fide* exercise of its police power; but the Federal Supreme Court construed it as in effect discriminating against the bringing in of liquors from other States, and as such, void as a hindrance to interstate commerce.[7]

No better summary of the scope of the power of the States over commerce, nor better examples of proper and improper State regulations thereof, can be found than in the following quotation from the leading case of Covington Bridge Co. v. Kentucky:[8]

"The adjudications of this court with respect to the power of the States over the general subject of commerce are divisible into three classes: *First,* those in which the power of the state is exclusive; *second,* those in which the States may act in the absence of legislation by Congress; and *third,* those in which the action of Congress is exclusive and the States cannot interfere at all.

"The first class, including all those wherein the States have plenary power, and Congress has no right to interfere, concern the strictly internal commerce of the State, and while the regulations of the State may affect interstate commerce indirectly, their bearing upon it is so remote that it cannot be termed in any just sense an interference. Under this power, the States may authorize the construction of highways, turnpikes, railways, and canals between points in the same State, and regulate the tolls for the use of the same.....and may authorize the building of bridges

[6] Brennan v. Titusville, 153 U. S. 289. [8] 154 U. S. 204.
[7] Scott v. Donald, 165 U. S. 58.

over non-navigable streams, and otherwise regulate the navigation of the strictly internal waters of the State—such as do not, by themselves or by connection with other waters, form a continuous highway over which commerce is or may be carried on with other States or foreign countries.....This is true, notwithstanding the fact that the goods or passengers carried or traveling over such highway between points in the same State may ultimately be destined for other States, and, to a slight extent, the State regulations may be said to interfere with interstate commerce. The States may also exact a bonus, or even a portion of the earnings of such corporation, as a condition to the granting of its charter . . . Under this power the States may also prescribe the form of all commercial contracts, as well as the terms and conditions upon which the internal trade of the State may be carried on.

"Within the second class of cases—those of what may be termed concurrent jurisdiction—are embraced laws for the regulation of pilots; . . . quarantine and inspection laws and the policing of harbors; . . . the improvement of navigable channels; . . . the regulation of wharves, piers, and docks; . . . the construction of dams and bridges across the navigable waters of a State; . . . and the establishment of ferries. . . . Of this class of cases it was said by Mr. Justice Curtis in Cooley v. Philadelphia Port Wardens: 'If it were admitted that the existence of this power in Congress, like the power of taxation, is compatible with the existence of a similar power in the States, then it would be in conformity with the contemporary exposition of the Constitution, and with the judicial construction, given from time to time by this court, after the most deliberate consideration, to hold that the mere grant of such a power to Congress did not imply a prohibition on the States to exercise the same power; that it is not the mere existence of such a power, but its exercise by Congress, which may be incompatible with the exercise of the same power by the States, and that the States may legislate in the absence of Congressional regulations.' . . . But even in the matter of building a bridge, if Congress chooses to act, its action necessarily supersedes the action of the State. . . . As matter of fact, the building of bridges over waters dividing two States is now usually done by Congressional sanction. Under this power the States may also tax the instruments of interstate commerce as it taxes other similar property, provided such tax be not laid upon

the commerce itself. But wherever such laws, instead of being of a local nature and not affecting interstate commerce but incidentally, are National in their character, the non-action of Congress indicates its will that such commerce shall be free and untrammelled, and the case falls within the third class of those laws wherein the jurisdiction of Congress is exclusive. . . . Subject to the exceptions above specified, as belonging to the first and second classes, the States have no right to impose restrictions, either by way of taxation, discrimination, or regulation, upon commerce between the States. That, while the States have the right to tax the instruments of such commerce as other property of like description is taxed, under the laws of the several States, they have no right to tax such commerce itself, is too well settled even to justify the citation of authorities. The proposition was first laid down in Crandall v. Nevada[9] and has been steadily adhered to since. That such power of regulation as they possess is limited to matters of a strictly local nature, and does not extend to fixing tariffs upon passengers or merchandise carried from one State to another, is also settled by more recent decisions, although it must be admitted that cases upon this point have not always been consistent."

Of other subjects to which local and special regulation are applicable, so long as Congress has passed no conflicting laws upon the same subject, the following may be taken as typical: the hours during which a bridge over the Chicago River may be opened;[10] the protection of the game of a State, even to the extent of forbidding the killing of it for shipment out of the State;[11] the use of the arms or great seal of a State for advertising purposes.[12] All these subjects are principally matters of local concern, and their regulation by the several States is generally justified in the theory that the legislation is in fact an aid to commerce. Whether, however, aids to commerce or checks upon it, such local regulations constitute no interference with the

[9] 6 Wall. 35.

[10] Escanaba Transp. Co. v. Chi., 107 U. S. 678; Cardwell v. Amer. Bridge Co., 113 U. S. 205.

[11] Geer v. Conn., 161 U. S. 519.

[12] Com. v. R. I. Sherman Mfg. Co., 189 Mass. 76.

commercial power of Congress for the reason that when Congress acts the State authority is superseded.[13]

§ 18. State Police Power as Affecting Commerce. Aside from purely local regulations, if State legislation affects commerce that is within the commerce clause, it must in the last analysis be justified as an enactment of the police power of the State,[14] and must, in addition, not conflict with any Act of Congress. Just what this police power is it is difficult to say with any degree of definiteness. "It is generally said to extend to making regulations promotive of domestic order, morals, health, and safety. . . . All these exertions of power are in immediate connection with the protection of persons and property against noxious acts of other persons, or such a use of property as is injurious to the property of others. They are self-defensive."[15]

Promotion of Public Health. The power to legislate for the protection of their citizens is reserved to the several States. In order to secure the general health and welfare of its people, a State may, therefore, adopt precautionary measures against disease by excluding from its limits persons or property having contagious or infectious diseases.[16] It may provide that whoever permits diseased cattle in his possession to run at large in the State shall be liable for any damages caused by the spread of the disease occasioned thereby.[17] Quite apart from the desirability of preventing fraud and deception, and equal justification for the police laws affecting interstate commerce, a State may insure the purity of imported coffee by prohibiting the bringing in of coffee so adulterated as to conceal damage.[18] But while a State may forbid altogether the manufacture or sale of oleomargarine colored in imitation of butter,[19] it

[13] Mobile County v. Kimball, 102 U. S. 691; Gilman v. Phila., 3 Wall. 713; Cardwell v. American Bridge Co., 113 U. S. 205.

[14] Robbins v. Shelby County Tax Distr., 120 U. S. 489.

[15] R. R. v. Husen, 95 U. S. 465, 470.

[16] R. R. v. Husen, 95 U. S. 465.

[17] Brimmer v. Rebman, 138 U. S. 78.

[18] Crossman v. Lurman, 192 U. S. 189.

[19] Plumley v. Mass., 155 U. S. 461.

cannot forbid the importation of a legitimate article of commerce merely because a great deal of it is adulterated and made unwholesome by dishonest manufacturers.[20] For these same purposes, and quite apart from the Constitutional grant of power to lay such duties on imports or exports as are necessary for executing their inspection laws,[21] the police power of the State includes power to pass reasonable and appropriate laws for the inspection of articles of interstate commerce.[22] That State quarantine and sanitary laws are upheld in the absence of conflicting legislation by Congress, is a matter of course requiring no citation of examples.[23] "The matter is one in which the rules that should govern it may in many respects be different in different localities, and for that reason be better understood and more wisely established by the local authorities. The practice which should control a quarantine station on the Mississippi River, a hundred miles from the sea, may be widely and wisely different from that which is best for the harbor of New York."[24]

Public Safety and Convenience. It is under the police power to provide for the public convenience and safety, that the numerous and familiar State regulations of railways and telegraph companies are most appropriately grouped. The scope of this section prevents more than a very few suggestive examples, from which the general principles involved are easily deducible.

A State may require all railway companies operating therein to cause three of their regular passenger trains each way, to stop daily at stations having over three thousand inhabitants, and may enforce such a law against interstate trains in the absence of any action by the Federal government.[25] But a State railroad commission has no power to

[20] Schollenberger v. Pa., 171 U. S. 1.

[21] Const. § 10, Art. I.

[22] Patapsco Guano Co. v. N. C. Board of Agric., 171 U. S. 345.

[23] Louisiana v. Texas, 176 U. S. 1; Higgins v. 300 Casks Lime, 130 Mass. 1; Brown v. Maryland, 12 Wheat. 419.

[24] Morgan's S. S. Co. v. La. Board of Health, 118 U. S. 455, 465.

[25] Lake Shore R. R. v. Ohio, 173 U. S. 285.

compel trains engaged mainly in interstate business, and running on fast schedule, to stop at every station, where the carrier has adequately supplied the needs of every locality by other means.[26]

Similar provisions are those consulting the convenience and comfort of the community with respect to the buildings, wires, and poles of telegraph companies, and those requiring the prompt receipt and delivery of messages from places either within or without the State;[27] but a State may not regulate the delivery outside the State of messages sent from within the State.[28]

"It has never been supposed that the dominant power of Congress over interstate commerce took from the States the power of legislation with respect to the instruments of such commerce, so far as the legislation was within its ordinary police powers. Nearly all the railways in the country have been constructed under State authority, and it cannot be supposed that they intended to abandon their power over them as soon as they were finished. The power to construct them involves necessarily the power to impose such regulations upon their operation as a sound regard for the interests of the public may seem to render desirable. In the division of authority with respect to interstate railways Congress reserves to itself the superior right to control their commerce and forbid interference therewith; while to the States remains the power to create and to regulate the instruments of such commerce, so far as necessary to the conservation of the public interests."[29]

Such rules as a State prescribed for the construction, management, and operation of railroads, accordingly, with a design to protect persons and property that would otherwise be endangered, are strictly within the police power,

[26] Comm. v. R. R. Co., 203 U. S. 335; R. R. v. Wharton, 207 U. S. 328, 28 S. Ct. 121. See also H. & T. C. R. R. v. Mayes, 201 U. S. 321, 329, 50 L. ed. 775; St. Louis S. W. R. R. v. State of Ark., 217 U. S. 136, 54 L. ed. 698, 29 L. R. A. (N. S.) 802.

[27] W. U. Tel. Co. v. Pendleton, 122 U. S. 347.

[28] W. U. Tel. Co. v. James, 162 U. S. 650.

[29] *Per* Brown J. in Louisville R. R. v. Ky., 161 U. S. 677, 702.

providing they do not directly burden, impede, or impair the usefulness of interstate commerce.[30] A State, for instance, may require the physical examination and licensing of engineers and other persons engaged in the driving and management of interstate trains;[31] may regulate the speed of trains in or near cities and towns or at crossings;[32] may require railroads to light their roads within the limits of municipalities by electricity;[33] may prescribe the mode of heating passenger cars in the State, even though the cars be engaged in interstate commerce. Said Mr. Justice Harlan in this last decision:[34]

"Inconveniences of this character cannot be avoided so long as each State has plenary authority within its territorial limits to provide for the safety of the public, according to its own views of necessity and public policy, and so long as Congress deems it wise not to establish regulations on the subject that would displace any inconsistent regulations of the State covering the same ground."

In the absence of Federal legislation on the subject, a State may even regulate the liability of a common carrier, although interstate commerce be indirectly affected.[35] The carrier's argument that the subject being interstate commerce admitted of no State action, and that there being no Federal legislation and no Federal common law, it was free to limit its liability in consideration of the giving of a cheaper rate, overlooked the fact, said the court, that the journey within the State was within the control of the police power of the State, and the State, accordingly, might as to such part of the journey, forbid limitations of liability, through express legislation or recognition of common law.[36]

In subserving the public convenience, a State may pro-

[30] Ill. Cent. R. R. v. Ill., 163 U. S. 142.
[31] Mo. v. Haber, 169 U. S. 613, 633; Nashville R. R. v. Alabama, 128 U. S. 96.
[32] Erb v. Morasch, 177 U. S. 584.
[33] St. Bernard v. Cleveland R. R., 4 Ohio Dec. 371.
[34] N. Y. R. R. v. N. Y., 165 U. S. 628, 633.
[35] Martin v. R. R., 203 U. S. 284.
[36] W. U. Tel. Co. v. Call Pub. Co., 181 U. S. 92; Chi. R. R. v. Sloan, 169 U. S. 133; Pa. R. R. v. Hughes, 191 U. S. 477.

hibit the sale of railway tickets by others than specially authorized agents;[37] may prohibit a railroad company from acquiring any parallel or competing line;[38] may penalize railroads for refusal to receive freight tendered for transportation.[39] All these are legitimate exercises of the police power of the State to regulate the instruments of interstate commerce, so far as necessary to the conservation of the public safety and convenience. Such regulations, affording as they do facilities to interstate commerce, do not regulate such commerce within the meaning of the Constitution, unless in particular cases they conflict with Acts of Congress.[40] But a State statute, however convenient, authorizing attachment process upon a freight car loaded with interstate freight, is a direct interference with commerce, and is contrary to the letter of the commerce clause.[41]

Protecting Public Morals and Suppressing Social Evils. Public morals, social evils, and the maintenance of good order in the commonwealth, are proper subjects for State regulation, even though interstate commerce be also indirectly affected. The extent, however, to which State police legislation may affect commerce is a question necessarily indefinite and upon which there is not complete harmony of opinion. The following cases are illustrations of the principle involved. In Hennington v. Georgia,[42] a statute declaring that the transportation of freight should be suspended on Sunday, under certain conditions and exceptions, was upheld as a part of the policy of the State designed to promote the general welfare of its people. To exclude criminals and paupers,[43] to guard against deception and fraud through adulteration of articles of commerce,[44] to forbid the sale of lottery tickets—although such tickets are to be

[37] State v. Thompson, 84 Pac. (Ore. 1906) 476; compare People *ex rel.* v. City Prison, 157 N. Y. 116.

[38] Louisville R. R. v. Ky., 161 U. S. 677.

[39] Currie v. Raleigh Air Line R. Co., 135 N. C. 535.

[40] Wis. R. R. v. Jacobson, 179 U. S. 287.

[41] Wall v. Norfolk R. R., 52 W. Va. 485.

[42] 163 U. S. 299.

[43] Ames v. Kirby, 71 N. Y. L. 442; Hannibal R. R. v. Husen, 95 U. S. 465.

[44] Plumley v. Mass., 155 U. S. 461; Crossman v. Lurman, 192 U. S. 189.

drawn in another State[45]—are all within the police power, though interstate commerce be also affected.

Precautionary measures against disease and social evils are eminently proper in the exercise of the police power. State laws designed to avoid the spread of contagious diseases have been upheld.[46]

In many of the southern States there is legislation separating negroes and whites in public resorts and conveyances. In the leading case of Hall v. De Cuir,[47] the legislation questioned belonged to the more liberal class, requiring equal privileges for all passengers, irrespective of color, instead of demanding separate accommodations. However, when applied to a steamboat plying navigable waters of the United States, crossing now to one State shore, now to another, the law was held unconstitutional as a direct burden upon interstate commerce. It would seem, then, that the State laws demanding separation of blacks and whites, if framed so as to apply to interstate carriage, must share the same fate. The power to regulate racial relations, however, must not be exercised so as to affect or burden unduly interstate commerce, irrespective of whether Congress has passed any similar laws itself or not. Whether these State laws requiring separation of passengers deal with a subject admitting "only of one uniform system", so far as interstate commerce is concerned, is a question upon which the cases are in conflict. Thus the court in Tennessee declared that the States have power to control the situation; that however correct the Federal Supreme Court was in holding bad the Louisiana statute prohibiting separation, a law demanding separation is a valid police regulation and applies both to intra and interstate travel.[48] The court says that there was no mention of "police power" in Hall v. De Cuir, and that the question, therefore, is still an open one. But the Supreme Court undoubtedly meant to decide

[45] Roselle v. Farmer's Bank, 141 Mo. 36.
[46] Hannibal R. R. v. Husen, 95 U. S. 465.
[47] 95 U. S. 485.
[48] Smith v. Tenn., 100 Tenn. 494; 41 L. R. A. 430.

just what it did—that laws regulating the relations between the races, no matter what called, are bad when applied to interstate commerce. It is true that the Supreme Court has not directly passed upon the constitutionality of a State statute demanding separation of black and white interstate passengers; but in C. O. R. R. v. Ky.,[49] decided in 1900, two years after Smith v. Tennessee, the Court clearly intimates it would hold the so-called Jim Crow legislation bad if applied to interstate commerce. In a short opinion, as previously noted, the sole point made was that as the Kentucky court had construed the particular enactment as applying only to transportation between points in that State, this construction was binding upon the Supreme Court, and the law was held valid. This decision entirely takes away the basis of the Tennessee court's reliance on several *dicta* of Mr. Justice Harlan's in the Hennington case;[50] and, also, in N. Y., N. H. & Hartford R. R. v. N. Y.,[51] where he said that in the reasonable exercise of the police power a State may impose burdens upon interstate commerce which occasion both inconvenience and hardship to the carrier, provided Congress has not directly acted upon the same subject.

Reasonableness of Police Laws Affecting Commerce. A State police law affecting interstate commerce, although it does not invade the exclusive jurisdiction of Congress, and does not in its operation conflict with any legislation of Congress, may nevertheless be attacked as unreasonable, and as repugnant, therefore, to "due process of law" under the Fourteenth Amendment. To lay down any exact rule whereby it may be determined whether a police law is unreasonable is of course as impossible as it is to define exactly the police power itself. Any "reasonableness" test must necessarily be unsatisfactory, for one man will not only find unreasonable in his own eyes what another man will deem proper, but will say that the other man is unreasonable for deeming it proper. Accordingly, the test ap-

[49] 179 U. S. 388.
[50] Hennington v. Ga., 163 U. S. 299.
[51] 165 U. S. 628.

plied by the courts is not whether they would have passed this particular sort of legislation; but whether, viewing the subject rationally, the legislative determination in its favor is a reasonable and permissible one. As illustrating the length to which the presumption of reasonableness of the legislation will be indulged in a *dictum* in a recent Wisconsin case is of interest:

"As to the cogency or propriety of either the regulations made, or the importance of the distinctions, as we have so often said, the courts have little concern. Those subjects rest with the legislature, and only when the court, in the exercise of the utmost deference toward that other branch of the government, is compelled to say that no one in the exercise of human reason and discretion could honestly reach a conclusion that distinctions exist having any relation to the purpose and policy of the legislation, can it deny it validity." [52]

These police laws must, of course, have some real or substantial relation to the object for which they are enacted. While a State may impose a liability upon persons transporting infected cattle,[53] it may not go beyond its necessary self-protection by excluding all cattle coming from a certain place at certain seasons whether diseased or not.[54] Said Mr. Justice Strong in the latter case:

"The Missouri statute is a plain interference with such transportation, an attempted exercise over it of the highest possible power—that of destruction. It meets at the borders of the State a large and common subject of commerce, and prohibits its crossing the State line during two-thirds of each year, with a proviso, however, that such cattle may come across the line loaded upon a railroad car or steamboat, and pass through the State without being unloaded. But even the right of steamboat owners and railroad companies to transport such property through the State is loaded by the law with onerous liabilities, because of their agency in the transportation. The object and effect of the

[52] Mr. Justice Dodge, in State v. Evans, 110 N. W. 241.
[53] Mo. R. R. v. Haber, 169 U. S. 613.
[54] Hannibal R. R. v. Husen, 95 U. S. 465, 470.

statute are, therefore, to obstruct interstate commerce, and to discriminate between the property of citizens of one State and that of citizens of other States."

Although every reasonable presumption will be indulged in favor of a police law affecting interstate commerce, that its reasonableness is a subject of closer scrutiny than the words of the Wisconsin case quoted above might lead one to infer, is indicated in the case of Houston R. R. v. Mayes.[55] A Texas statute imposed a penalty upon railroads which, except in case of "strikes or other public calamity", should fail to furnish cars to shippers within a certain number of days on receipt of written requisition therefor and the deposit of one-fourth of the freight charges. In holding the law invalid as applied to cars required for interstate shipments, Mr. Justice Brown emphasizes its unreasonableness in the following words:

"We think an absolute requirement that a railroad shall furnish a certain number of cars at a specified day, regardless of every other consideration except strikes and other public calamities, transcends the police power of the State and amounts to a burden upon interstate commerce. It makes no exception in cases of a sudden congestion of traffic, and actual inability to furnish cars by reason of their temporary and unavoidable detention in other States, or in other places within the same State. It makes no allowance for interference of traffic occasioned by wrecks or other accidents upon the same or other roads, involving a detention of traffic, the breaking of bridges, accidental fires, washouts, or other unavoidable consequences of heavy weather. . . . While railroad companies may be bound to furnish sufficient cars for their usual and ordinary traffic, cases will inevitably arise where by reason of an unexpected turn in the market, a great public gathering, or an unforeseen rush of travel, a pressure upon the road for transportation facilities may arise, which good management and a desire to fulfil all its legal requirements cannot provide for, and against which the statute in question makes no allowance."

The cases requiring the stopping of trains, cited in a pre-

[55] 201 U. S. 321, 329.

vious section,[56] are further illustrative of the attention to particular facts demanded when the unreasonableness of a police law is the issue.

§ 19. Discriminatory State Statutes. Neither by police laws nor by taxation, nor in any other manner, may a State impose more onerous burdens upon persons or goods engaged in interstate commerce than it imposes upon the like persons or goods of its own territory.

"If this were not so, it is easy to perceive how the power of Congress to regulate commerce with foreign nations and among the several States could be practically annulled, and the equality of commercial privileges secured by the Federal Constitution to citizens of the several States be materially abridged and impaired."[57]

Accordingly an ordinance of the city of Baltimore, allowing free use of its wharves to vessels carrying Maryland products and charging vessels carrying the products of other States, was held invalid although the charge made was not in excess of reasonable compensation for the use of the city's property.[58] In the leading case of Welton v. Missouri,[59] that State had enacted a law declaring all persons going from place to place to sell goods and merchandise not the products of Missouri, to be peddlers, and imposing a penalty for failure to procure a license as such. The law was held to be in conflict with the constitutional principle which forbids the imposition of burdens upon articles by reason of their foreign origin, even after they have entered the State. "It was against legislation of this discriminating kind that the framers of the Constitution intended to guard when they vested in Congress the power to regulate commerce among the several States."[60]

[56] Compare also Cleveland R. R. v. Ill., 177 U. S. 514; Gladson v. Minn., 166 U. S. 427; Ill. Cent. v. Ill., 163 U. S. 142.

[57] Guy v. Baltimore, 100 U. S. 434, 439.

[58] See *supra*, footnote 57. *Semble*, license fee imposed on outside manufacturers for warehouses in state, Minneapolis Brewing Co. v. McGillivray, 104 Fed. 258.

[59] 91 U. S. 275.

[60] *Per* Mr. Justice Field, in Webber v. Va., 103, U. S. 344, 350.

Discriminatory, too, is a law prohibiting the having in one's possession liquors purchased outside the State, while permitting the possession of liquor purchased at a State dispensary,[61] or prohibiting citizens from importing liquors from other States while permitting such importation by State officials.[62] To restrict to State officials the privilege of importing liquors for sale, however, is not discriminating, as any citizen may still import for his own use.[63] For similar reasons the so-called "Dow Law" of Ohio, which in effect exempted from certain taxation the sale of intoxicating liquors made by the manufacturer at the factory, was upheld as imposing no discrimination upon factories in other States, since the exemption applied to all factories in the State whether or not owned by Ohio residents, and the tax was imposed not merely on foreign manufacturers desiring to sell liquor in Ohio, but also on Ohio corporations with breweries in other States or with salesplaces in Ohio distinct from their factories.[64]

Care must be taken in the framing even of inspection laws that they do not operate as a discriminatory burden against the citizens of other States. A Minnesota statute providing that all beef should be inspected by the proper officer twenty-four hours before the animals were slaughtered, while well intended, in effect necessarily excluded from Minnesota markets all meat taken from animals slaughtered in other States, and accordingly was invalid. The same was held as to the Virginia law making it unlawful to sell, without inspection and payment of fee therefor, meat from animals slaughtered more than one hundred miles from the place of sale.[65] Much power is reserved to a State, even over interstate commerce; but it "may not,

[61] State v. Holleyman, 55 S. C. 207, 31 S. E. 362, 33 S. E. 366, 45 L. R. A. 567.

[62] Donald v. Scott, 67 Fed. 854.

[63] Vance v. W. A. Vandercook Co., 170 U. S. 438, 18 S. Ct. 674, 42 L. ed. 1100.

[64] Reymann Brewing Co. v. Brister, 179 U. S. 445, 21 S. Ct. 201, 45 L. ed. 269.

[65] Minnesota v. Barber, 136 U. S. 313; Brimmer v. Rebman, 138 U. S. 78.

under the guise of exerting its police powers, or of enacting inspection laws, make discriminations against the products and industries of some of the States in favor of the products and industries of its own or of other States."[66]

§ 20. When Commerce Becomes Immune from State Law. When an article of commerce has lawfully begun to move upon its final journey from one State to another, or from or to a foreign country, the power of Congress under the commerce clause becomes operative. To render articles of commerce immune from State regulation, such as taxation by the State, preparation of them for interstate or foreign shipment is not sufficient; by the mere intent of the manufacturer to export them they are no more separated from the general mass of property in the State than are manufactured articles.[67] In Coe v. Errol the question before the court was whether certain logs cut at a place in New Hampshire, and hauled to a river town in the same State for the purpose of being floated down the river to the State of Maine, were liable to be taxed like other property in the State of New Hampshire. In deciding that they were, while the logs cut in the State of Maine, were not, the court declared:

"There must be a point of time when they cease to be governed exclusively by the domestic law and begin to be governed and protected by the National law of commercial regulation, and that moment seems to us to be a legitimate one for the purpose, in which they commence their final movement for transportation from the State of their origin to that of their destination. When the products of the farm or the forest are collected and brought in from the surrounding country to a town or station serving as an entrepôt for that particular region, whether on a river or a line of railroad, such products are not yet exports, nor are they in process of exportation, nor is exportation begun until they are committed to the common carrier for transportation out of the State to the State of their destination, or have started on their ultimate passage to that State. Until then it is reasonable to regard them as not only within

[66] *Per* Mr. Justice Harlan, in Brimmer v. Rebman, 138 U. S. 78, 82.
[67] Coe v. Errol, 116, U. S. 517, 525; Kidd. v. Pearson, 128 U. S. 1.

the State of their origin, but as a part of the general mass of property of that State, subject to its jurisdiction, and liable to taxation there, if not taxed by reason of their being intended for exportation, but taxed without any discrimination, in the usual way and manner in which such property is taxed in the State."

Exportation, actual or constructive, is required, and this is not begun until the goods are committed to a carrier for transportation out of the State to the State of their destination, or until they have actually started on their ultimate passage to that State. The interstate journey once begun, its character is not destroyed by delays or detentions. Thus a dining car engaged in interstate commerce is still under the control of Congress while waiting for the train to be made up between trips.[68] But if the journey is stopped, not for a mere incidental purpose, but for a collateral one, such as to make a sale, the protection of the commerce clause has ceased. In the recent case of General Oil Company v. Crane, the material facts were as follows: A Tennessee corporation, engaged in the manufacture and sale of coal oil in the various States of the Union, with its principal plants in Pennsylvania and Ohio, maintained a shipping depot at Memphis, at which oil was unloaded from tank cars into various tanks, barrels, and other receptacles, and thence forwarded, as ordered, to its final destination. The court held that the oil at the distributing depot, under these circumstances, was not "property in interstate commerce", and was, therefore, subject to the inspection and taxing laws of the State of Tennessee.[69] For a similar reason, where a carrier had delivered interstate goods to the destination named in the bill of lading, the consignee could not continue the protection of the commerce clause by ordering the goods at once shipped over the line of a connecting carrier to another point in the State. On delivery to the original consignee, the interstate transaction was completed.[70]

[68] Johnson v. So. Pac. R. R., 196 U. S. 1.
[69] General Oil Co. v. Crain, 209 U. S. 211.
[70] R. R. Co. v. Texas, 204 U. S. 403, 27 Sup. Ct. 360, 51 L. ed 540.

§ 21. When State Power Becomes Operative. The commerce clause ceases to apply when articles of commerce become a part of the general mass of property in a State. This generally happens either when the importer has sold the goods in the original package, or the original package (a phrase to be later defined) has been broken. An article does not cease to be a subject of interstate commerce the instant it enters the State of its destination; the power of the State over the article does not begin until the importer has so acted upon it that it has become incorporated with the mass of property of the State.[71] The reason of the rule is self-evident; could State legislation restrict such articles before such incorporation the very object of the framers of the Constitution in vesting control in Congress would be defeated.[72] For the power of the State to attach, the goods must not merely have reached their destination, but must have been actually or constructively delivered to the consignee, and by him acted upon in the manner later described.[73] If a freight train containing interstate traffic has arrived at its destination but still remains on the tracks of the railway company, and has not yet been delivered to the consignee, the interstate transportation of the property has not been completed, and the regulating power of the State has not begun.[74]

[71] Gibbons v. Ogden, 9 Wheat. 1; Brown v. Maryland, 12 Wheat. 419.
[72] Welton v. Missouri, 91 U. S. 275, 281.
[73] Heyman v. R. R. Co., 203 U. S. 270, 27 Sup. Ct. 104, 51 L. ed. 178.
[74] McNeill v. So. R. R., 202 U. S. 543.

CHAPTER IV

STATE TAXATION

§ 22. Limitations Of. The foregoing principles are applicable to such general State regulations of commerce as have been previously discussed. As regards taxation of the article of commerce a distinction must be drawn between the protection afforded by the commerce clause and by the import clause of the Constitution. While the question of taxation will be discussed in the next section, it is proper to notice here the different principles to be applied to taxation of goods in the original packages that have come from a foreign country, and those that have come from another State. The former are "imports", within the meaning of the clause of the Constitution that "no State shall, without the consent of Congress, lay any imposts or duties on imports or exports," and, therefore, cannot be taxed, even after arrival in a State, so long as they are in the original package.[1] Goods sent into one State from another, on the other hand, are not "imports" in this sense, and are not under the protection of the clause of the Constitution just quoted. That the protection from taxation afforded to imports is more extensive than to commodities coming from one State to another, although in the original package, is brought out by the case of Brown v. Houston.[2] With regard to the taxation of coal mined in Pennsylvania and sent into Louisiana, where, while afloat on the Mississippi, it was offered for sale, the court declared:

"The coal had come to its place of rest, for final disposal or use, and was a commodity in the market of New Orleans. It might continue in that condition for a year or two years,

[1] Woodruff v. Parham, 8 Wall 123; Brown v. Maryland, 12 Wheat. 419.
[2] 114 U. S. 622, 632.

or only for a day. It had become a part of the general mass of property in the State, and as such it was taxed for the current year, as all other property in the city of New Orleans was taxed."

Similarly, where coal barges destined for Baton Rouge were, for the owner's convenience, moored in the Mississippi about nine miles above the city, and there offered for sale, it was held that the property had become subject to State taxation, though still in the original package.[3] If these same coal barges had come from Mexico or some other foreign country and had been, therefore, technically speaking, imports they would not have been subject to State taxation until the original package (in this case the barge) was broken, or until there had been a sale. As will be presently pointed out, an import does not, for purposes of taxation, become mingled with the mass of property in a State as soon as commodities from other States.

While a sale of the property after it has reached destination is held to constitute a commingling with the mass of property of the State and to mark the time when State regulation may become operative, it is nevertheless possible to show that an article has lost its interstate character in other ways. This is clearly indicated in the case of Brown v. Houston mentioned above.

§ 23. Validity Of. In the preceding section was mentioned the distinct limitations placed upon the taxing power of the State, *first,* by the import clause, and *second,* by the commerce clause itself. The former, it will be remembered, provides that "no State shall, without the consent of Congress, lay any imposts or duties on imports or exports". As here used, the word "imports" has a technical meaning, referring only to articles imported from foreign countries. The prohibition does not refer to interstate commerce at all.[4] But, as construed by Mr. Chief Justice Marshall in Brown v. Maryland, it does apply to articles imported from foreign countries, and prevents State taxation of them so

[3] Pitts. Coal Co. v. Bates, 156 U. S. 577.
[4] Patapsco Guano Co. v. N. C., 171 U. S. 345.

long as they are in the original package.[5] While, therefore, the incorporation of "imports" in the general mass of property of the State comes later, as far as the power to tax is concerned, that is, while foreign goods until sold by the importer or otherwise incorporated with the mass of property in the State, are immune from State taxation,[6] the status of goods brought in from another State is, for purposes of taxation, to be considered independent of this clause of the Constitution, and under the familiar and previously discussed principles of the commerce clause itself.

Since a State may not impose a burden upon interstate commerce, it may not lay a tax upon interstate commerce in any form, whether by way of duties laid upon interstate transportation, on the receipts of that transportation, or on the business of conducting interstate commerce itself.[7] In Welton v. Missouri, already mentioned, the plaintiff in error, who was a dealer in sewing machines manufactured outside of the State of Missouri, was indicted under a statute of that State for peddling foreign made goods without a license, no license being required of peddlers of Missouri-made goods. Said the court:

"Where the business or occupation consists in the sale of goods, the license tax required for its pursuit is in effect a tax upon the goods themselves. If such a tax be within the power of the State to levy, it matters not whether it be raised directly from the goods, or indirectly from them through the license to the dealer; but, if such tax conflict with any power vested in Congress by the Constitution of the United States, it will not be any the less invalid because enforced through the form of a personal license . . . It is sufficient to hold now that the commercial power (of the Federal Government) continues until the commodity has ceased to be the subject of discriminating legislation by reason of its foreign character. That power protects it, even after it has entered the State, from any burdens

[5] Brown v. Maryland, 12 Wheat. 419.

[6] Waring v. Mobile, 8 Wall. 10; Low v. Austin, 13 Wall. 29; May v. New Orleans, 178 U. S. 496; Woodruff v. Parham, 8 Wall. 123.

[7] State Freight Tax Case, 15 Wall. 232; Welton v. Missouri, 91 U. S. 275; Bowman v. Chi. R. R., 125 U. S. 496; McCall v. Cal., 136 U. S. 104.

imposed by reason of its foreign origin. The Act of Missouri encroaches upon this power in this respect, and is, therefore, in our judgment, unconstitutional and void."[8]

If the State of Missouri had laid a tax upon all sewing machines, irrespective of where they were made, as a part of her general scheme for the taxation of personal property within her limits such a tax would have been valid. It should be noticed that in the case above discussed the tax was only upon the peddlers selling machines made outside of Missouri. No license fee was exacted of peddlers of domestic goods. The tax on the privilege of selling an article is equivalent to tax on the article itself. The tax in question, therefore, discriminated against foreign goods in favor of domestic goods, and thus constituted a burden on interstate commerce in such commodities.

That the general rule is that a State may not, by the taxation, impose any burden upon interstate commerce, is undoubted, but it is at once obvious that there is much taxation of goods that are or have been the subjects of interstate commerce, that does not constitute a tax on commerce. Goods actually in transit from one State to another are, to be sure, not taxable by any State; but they are not in process of transit, so as to be immune from State taxation, if they have been merely prepared for transportation and not yet started upon their continuous interstate journey.[9]

Once having arrived at their destination—and herein lies their difference from goods imported from foreign countries—goods transported from another State are taxable like other property in the State, even though still remaining in the original package.[10]

"It cannot be seriously contended, at least in the absence of any congressional legislation to the contrary, that all goods which are the product of other States are to be free

[8] Welton v. Missouri, 91 U. S. 275, 278, 282.

[9] Coe v. Errol, 116 U. S. 517; see *infra*, as to duration of protection of commerce clause, p. 66.

[10] Brown v. Houston, 114 U. S. 622; American Steel Co. v. Speed, 192 U. S. 500.

from taxation in the State to which they may be carried for use or sale. Take the city of New York, for example. When the assessor of taxes goes his round, must he omit from his list of taxables all goods which have come into the city from the factories of New England and New Jersey, or from the pastures and grainfields of the West? If he must, what will be left for taxation? And how is he to distinguish between those goods which are taxable and those which are not? With the exception of goods imported from foreign countries, still in the original packages, and goods in transit to some other place, why may he not assess all property alike that may be found in the city, being there for the purpose of remaining there till used or sold, and constituting part of the great mass of its commercial capital, provided always, that the assessment be a general one, and made without discrimination between goods the product of New York, and goods the product of other States? . . . We do not mean to say that if a tax collector should be stationed at every ferry and railroad depot in the city of New York, charged with the duty of collecting a tax on every wagon load, or car load of produce and merchandise brought into the city, that it would not be a regulation of, and restraint upon interstate commerce, so far as the tax should be imposed on articles brought from other States. We think it would be, and that it would be an encroachment upon the exclusive powers of Congress. It would be very different from the tax laid on auction sales of all property indiscriminately, as in the case of Woodruff v. Parham, which had no relation to the movement of goods from one State to another."[11]

On the arrival of goods at their destination, the State, in return for the protection it affords them, is entitled to some revenue for its support, even though by the tax, interstate commerce is in some measure affected. On the same principle of protection, instrumentalities of commerce having a *situs* in a State may be taxed although they belong to persons engaged in the transacting of interstate commerce and are used therein, so long as the tax is essentially only a property tax.[12] It is not a property tax, and is invalid,

[11] *Per* Mr. Justice Bradley in Brown v. Houston, 114 U. S. 622, 633, 634.

[12] American Refrigerator Co. v. Hall, 174 U. S. 70; Pullman Co. v. Pa., 141 U. S. 18; W. U. Tel. Co. v. Attorney-General, 125 U. S. 530.

if imposed upon a foreign railroad company engaged in interstate commerce, having no domicil in the State, and its property having no *situs* in the State otherwise.[13]

§ 24. Charges for Facilities Furnished. *Bona fide* and reasonable tolls for the use of improvements constructed under State authority are justified as being not taxes imposed irrespective of benefit returned, but as merely compensation for additional facilities furnished. Thus, in Huse v. Glover,[14] the State of Illinois adopted various measures for the improvement of the Illinois River, including the construction of a lock and dam at two places on the river, and charged tolls for the use of the improved waterway. The court upheld such charges, saying:

"The exaction of tolls for passage through the locks is as compensation for the use of artificial facilities constructed, not as an impost upon the navigation of the stream."

§ 25. Taxation of Imports and Exports. To any discussion of taxation of imports, it is proper to add that in the case of exports, a direct prohibition upon taxation by Congress is imposed by the Constitution. By article I, section 9, clause 5, it is provided: "No tax or duty shall be laid on articles exported from any State." This does not mean that Congress may not pass a general excise tax on all property of a certain kind alike, such as tobacco, even though the tobacco be manufactured under a contract for export, and be later actually exported. It is only when goods are taxed by reason of or on the occasion of their exportation, that the tax is repugnant to the Constitution as imposed on exports.[15] Further, the prohibition extends only to taxation of articles of foreign commerce, that is, articles exported to a foreign country; and a tax on goods for Porto Rico, would, therefore, not be a tax upon exports, as Porto Rico is not a foreign country.[16]

[13] Pickard v. Pullman Co., 117 U. S. 34, 24 Am. & Eng. R. Cas. 511; Tenn. v. Pullman Co., 117 U. S. 51; Indiana v. Pullman Co., 11 Bliss (U. S.) 561, 13 Am. & Eng. R. Cas. 307.

[14] 119 U. S. 543, 548.

[15] Fairbanks v. U. S., 181 U. S. 283; Cornell v. Coyne, 192 U. S. 419.

[16] Dooley v. U. S., 183 U. S. 151.

In the case of the States, the prohibition is contained in the clause:

"No State shall, without the consent of the Congress, lay any imposts or duties on imports or exports, except what may be absolutely necessary for executing its inspection laws; and the net produce of all duties and imposts, laid by any State on imports or exports, shall be for the use of the treasury of the United States; and all such laws shall be subject to the revision and control of the Congress."[17]

This, with the prohibition upon Congress previously quoted, forbids any tax on exports from the United States whatsoever. In the case of imports, as we have already seen, the clause refers only to goods coming from foreign countries; that goods coming from another State may, despite the commerce clause, be taxed at their destination like other property in the State.[18]

§ 26. State Inspection Laws. Now the question remaining is, what are these "inspection laws", to execute which, the Constitution, making an exception, allows the States to impose sufficient duties on exports and imports—at least in the absence of Congressional legislation. This question has been partly answered in the discussion of the powers of the States under the commerce clause. Under the latter, the power to pass inspection laws was construed as part of the police power of the State. The clause of the Constitution above quoted, is accordingly cumulative in this respect. Briefly stated, inspection laws should be "confined to such particulars as, in the estimation of the legislature and according to the customs of trade, are deemed necessary to fit the inspected article for the market, by giving to the purchaser public assurance that the article is in that condition, and of that quality, which makes it merchantable and fit for use or consumption."[19] In another leading case it was said:

"Recognized elements of inspection laws have always

[17] Const. Art. I., § 10, Cl. 2.

[18] Brown v. Maryland, 12 Wheat. 419; Woodruff v. Parham, 8 Wall. 123.

[19] Bowman v. Chi. R. R., 125 U. S. 465, 488.

been quality of the article, form, capacity, dimensions, and weight of package, mode of putting up, and marking and branding of various kinds, all these matters being supervised by a public officer having authority to pass or not pass the article as lawful merchandise, as it did or did not answer the prescribed requirements."[20]

For the efficient execution of these purposes, and to defray the expenses incident thereto, if Congress has not acted, the States may exact charges; but the charge must be imposed on personal property, not on persons. Therefore, a State law requiring immigrants to pay so-called inspection fees for determining whether they are criminals, paupers, or orphans, is invalid.[21] By necessary implication from the provision of the Constitution quoted, it is Congress that has the power to determine whether a State inspection charge is so high as to rebut the presumption it was imposed in good faith. In the latter case, the courts may interfere and declare the law not an inspection law at all, but designed for other purposes, and as repugnant to the Constitution either as in conflict with the commerce clause, or as undue process of law, or in some other manner.[22] "Congress may, therefore, interpose, if at any time any statute, under the guise of an inspection law, goes beyond the limit prescribed by the Constitution, in imposing duties or imposts on imports and exports."[23]

§ 27. Original Package Doctrine. From what has already been said as to the protection from State legislation which commodities enjoy either by virtue of the commerce clause or the import clause and as to the time when such protection ceases, it becomes necessary to refer to what is generally known as the original package doctrine. This so-called doctrine is a somewhat arbitrary test used to determine the time when a commodity becomes subject to the State regulation.

[20] Turner v. Maryland, 107 U. S. 38, 55.

[21] People v. Comp. Gen. Transatlantique, 107 U. S. 59, 61.

[22] Brimmer v. Redman, 138 U. S. 178; Patapsco Guano Co. v. N. C., 171 U. S. 355.

[23] Turner v. Maryland, *supra*.

State regulation, as has been pointed out, may take the form of police legislation in the interest of safety, health, and morals, or the form of taxation. As to State taxation, commodities, if they be, technically speaking, imports, that is, articles coming from a foreign country, are protected by both the commerce clause and by the import clause of the Federal Constitution. As to State police legislation, commodities coming from outside the State enjoy certain immunity by reason of the commerce clause. Thus the original package test is used not only in connection with protection against State taxation of imports, but also in connection with protection against State police legislation amounting to regulations of commerce. For example, a State tax on an imported article, or upon the right to sell it, is invalid, under the import clause, if the article is still in the original package. Likewise, a State police law forbidding the sale of intoxicating liquors is invalid, under the commerce clause, as to liquor coming from outside the State and offered for sale in the original package. The import clause secures to the importer the right to bring the article into the country and sell it once in the original package before the State can tax it. The commerce clause secures the right to send into a State an article of commerce and sell it once in the original package, before State police regulation can become operative. While selling once in the original package is a conclusive test of the termination of the Constitutional protection against State regulation or taxation, it is not an exclusive test. The importer or the shipper of an article into a State may in other ways destroy the immunity which such article enjoys; as, for example, by breaking the original package and mingling the contents thereof with other property within the State. And as to State taxation of articles coming from sister States, it has already been shown that such articles even, though still in the original package, may become so mingled with the mass of property within the State as to be subject to general nondiscriminatory State taxation.[24]

[24] See *supra*, § 22.

It becomes necessary to define, therefore, what constitutes an original package. The expression was first used by Mr. Chief Justice Marshall in Brown v. Maryland[25] in discussing the validity of a State license tax on sales by importers. The tax was held invalid as violating the import clause, and also, since the tax was discriminatory, as violating the commerce clause. No definition of what constitutes an original package was given. The fullest discus sion, and perhaps as definite a definition as is feasible, is found in the case of Austin v. Tennesee:[26]

"The defendant Austin purchased from the American Tobacco Company, at its factory in Durham, North Carolina, a lot of cigarettes manufactured by that company at that factory, and there, by it, put into pasteboard boxes, in quantities of ten cigarettes to each box; that each of these boxes, known as packages, was separately stamped and labeled, as prescribed by the United States revenue statute; that after defendant's purchase, the American Tobacco Company piled upon the floor of its warehouse, in Durham, North Carolina, the number of boxes or packages sold, and, having done so, notified the Southern Express Company to come and get them, and said company, by its agent, took them from the floor and placed them in an open basket already and previously in the possession of the Southern Express Company, and in that basket had them transported by express to the defendant's town in Tennessee, and there an agent of the same express company took the basket to defendant's place of business and lifted from it, on to the counter of the defendant the lot of detached boxes or packages of cigarettes, and thereupon took a receipt and departed with the empty basket. Thereafter the defendant sold one of these boxes or packages without breaking it."

He was convicted for violating the State law forbidding the sale of cigarettes. In deciding that the sale was not of an original package, and that, therefore, the defendant's conviction was proper, the majority of the court said:

"The real question in this case is whether the size of the package in which the importation is actually made is to

[25] 12 Wheat. 419. [26] 179 U. S. 343.

govern; or, the size of the package in which *bona fide* transactions are carried on between the manufacturer and the wholesale dealer residing in different States. We hold to the latter view. The whole theory of the exemption of the original package from the operation of State laws is based upon the idea that the property is imported in the ordinary form in which, from time to time immemorial, foreign goods have been brought into the country. These have gone at once into the hands of the wholesale dealers, who have been in the habit of breaking the packages and distributing their contents among the several retail dealers throughout the State. It was with reference to this method of doing business that the doctrine of the exemption of the original package grew up . . . In all the cases which have heretofore arisen in this court the packages were of such size as to exclude the idea that they were to go directly into the hands of the consumer, or be used to evade the police regulations of the State with regard to the particular article. No doubt the fact that cigarettes are actually imported in a certain package is strong evidence that they are original packages within the meaning of the law; but this presumption attaches only when the importation is made in the usual manner prevalent among honest dealers, and in a *bona fide* package of a particular size."[27]

In Schollenberger v. Pennsylvania,[28] ten-pound packages of oleomargarine were held to be original packages, the court relying upon a special verdict of the jury that the package was "of such form, size, and weight, as is used by producers or shippers for the purpose of securing both convenience in handling and security in transportation of merchandise between dealers in the ordinary course of actual commerce, and the said form, size, and weight were adopted in good faith, and not for the purpose of evading the laws of the Commonwealth of Pennsylvania."

If a dry-goods manufacturer puts one hundred separately wrapped packages of one dozen towels each into a large wooden case, which the importer opens, and then out of it offers for sale the separate unbroken packages of a dozen towels each, it is not the latter that constitute the original packages, but the large wooden packing case. Con-

[27] Austin v. Tenn., 179 U. S. 343, 359. [28] 171 U. S. 1, 20.

sequently, when this is opened, the separate small parcels are no longer immune from State taxation.[29] In the case of flour or grain shipped in carload lots, the goods in the sacks are the original packages.[30]

This principle, that the facts of the particular case may be scrutinized to determine whether the use of an original package of an unusual size for transportation, may not have been for the express purpose of evading or defying the police laws of the State, was attacked in Austin v. Tennessee, cited above, in the opinion of four dissenting justices, expressed by the late Mr. Justice Brewer as follows:

"Apparently, the dividing line as to the size of packages must be somewhere between that of a ten-pound package of oleomargarine and that of a package of ten cigarettes; but where? Must diamonds, in order to be within the protecting power of the Nation, be carried from State to State in ten-pound packages? If it be said that diamonds are not a subject of police regulation, and that a different rule obtains in reference to them than to matters of police regulation (as might be implied from the scope of the opinion), I can only say that the conclusion seems to me strange. Concretely, it amounts to this: The police power of the State, the power exercised to preserve the health and morals of its citizens, may prevent the importation and sale of a pint of whiskey, but cannot prevent the importation and sale of a barrel; or, in other words, the greater the wrong which is supposed to be done to the morals and health of the community, the less the power of the State to prevent it. That may be Constitutional law, but to my mind it lacks the saving element of common sense. I see no logical half-way place between a recognition of the power of the Nation to regulate commerce between the States in all things which are the subjects of commerce (in whatever form or manner they may be imported) and a concession of the power of the State to prevent absolutely the importation and sale of articles deemed by it prejudicial to the health or morals of its citizens."

§ 28. Assessing Property. In arriving at the value of property for purposes of taxation, a State is not limited

[29] May v. New Orleans, 178 U. S. 496.

[30] Lasater v. Purcell Mill Co., 22 Tex. Civ. App. 33

to the actual value of the tangible property, but may assess it on the value which it has when used, and which results from its use, notwithstanding that its increased value may result from use in interstate commerce. In Adams Express Co. v. Ohio State Auditor,[31] suits were brought by the express companies to restrain proceedings under a State statute to collect taxes from such companies, on the theory that the taxation was in violation of the commerce clause, in that, while purporting to be on the property of complainants within the State, was in fact levied on their business, which was largely interstate commerce. Said the court:

"Considered as distinct subjects of taxation, a horse is, indeed, a horse; a wagon, a wagon; a safe, a safe; a pouch, a pouch; but how is it that $23,430 worth of horses, wagons, safes, and pouches produces $275,446 in a single year? . . . The answer is obvious."

Then, in reply to the contention that as all the tangible property of the company in the United States combined was worth but $4,000,000, that amount was the limit of the combined taxing power of the various States in which it operated, the Supreme Court pointed out that the thing to be considered for the purposes of taxation is the proportionate part of the value, not of the mere tangible property alone, but of that resulting from the combination of the means whereby the business is conducted throughout the entire domain of operation.

"No fine-spun theories about *situs* should interfere to enable these large corporations, whose business is carried on through many States, to escape from bearing in each State such burden of taxation as a fair distribution of the actual value of their property among those States requires."[32]

In a similar case it was declared:

"The unit is a unit of use and management, and the

[31] 165 U. S. 194, 222.

[32] Adams Express Co. v. Ohio State Auditor, 166 U. S. 185, 225; see also Adams Express Co. v. Ky., 166. U. S. 171.

horses, wagons, safes, pouches, and furniture; the contracts for transportation facilities; the capital necessary to carry on the business, whether represented in tangible or intangible property, in Ohio, possessed a value in combination and from use in connection with the property and capital elsewhere, which could as rightfully be recognized in the assessment for taxation in the instance of these companies as the others. We repeat that while the unity which exists may not be a physical unity, it is something more than a mere unity of ownership. It is a unity of use, not simply for the convenience or pecuniary profit of the owner, but existing in the very necessities of the case—resulting from the very nature of the business.'"[38]

From this and similar situations in the case of railways and telegraph companies arises what is called the "unit rule", which simply stated is as follows. The property of corporations engaged in interstate commerce may be valued as a unit for the purposes of taxation, taking into consideration the uses to which it is put and all the elements making up its aggregate value. The proper proportion of the whole fairly ascertained may then be fairly taxed by the State without burdening interstate commerce. This proportion is generally ascertained by finding what proportion the mileage of, say, railroad or telegraph companies, operated within the State bears to the entire mileage operated both within and without the State. Or the proportion which the earnings from the business done within the State bears to the total earnings. To quote further from Adams Express Co. v. Ohio, it has been held:

"That a proper mode of ascertaining the assessable value of so much of the whole property as is situated in a particular State, is in the case of railroads, to take that part of the value of the entire road which is measured by the proportion of its length therein to the length of the whole; or taking as the basis of assessment such proportion of the capital stock of a sleeping-car company as the number of miles of railroad over which its cars are run in a particular State, bears to the whole number of miles traversed by them in that and other States; or such a pro-

[38] Adams Express Co. v. Ohio State Auditor, 165 U. S. 194, 222.

portion of the whole value of the capital stock of a telegraph company as the length of its lines within a State bears to the length of all its lines everywhere, deducting a sum equal to the value of its real estate and machinery subject to local taxation within the State."[34]

§ 29. Taxation of Franchises. Franchises, being privileges granted by a State at its pleasure, may be taxed as property by the State. In California v. Central Pacific Railroad Company,[35] the disputed point involved the validity of taxes assessed by the State of California upon the property of the railroad, including a franchise conferred by the United States. As to this franchise the tax was held invalid.

"Recollecting the fundamental principle that the Constitution, Laws, and Treaties of the United States are the Supreme Law of the land, it seems to us almost absurd to contend that a power given to a person or corporation by the United States may be subjected to taxation by a State."

Where, however, the franchise taxed by the State is a State franchise, "it is not to be denied that such rights and privileges have value and constitute taxable property."[36] So even though a State corporation be engaged in interstate commerce, a tax upon its franchise is not to be regarded as a tax upon commerce, but as a tax upon the State-created property, and as such it will be sustained if limited to the value of the franchise as property and to the value of the property of the corporation in the State.[37] While this does not include the right to tax a franchise granted by Congress,[38] it does include a right to tax all corporations, although organized in other States, in an amount proportioned to their capital stock without

[34] Adams Express Co. v. Ohio State Auditor, 165 U. S. 194, 221; Pullman Co. v. Pa., 141 U. S. 18; W. U. Tel. Co. v. Taggart, 163 U. S. 1.

[35] 127 U. S. 1, 41.

[36] Cent. Pac. R. R. v. Cal., 162 U. S. 91, 126.

[37] Henderson Bridge Co. v. Ky., 166 U. S. 150; Maine v. Grand Trunk R. R., 142 U. S. 217; Del. R. R. Tax, 18 Wall. 206; N. Y. v. Miller, 202 U. S. 584.

[38] Cal. v. Cent. Pac. R. R., 127 U. S. 1; Keokuk Bridge Co. v. Ill., 175 U. S. 627; Cent. Pac. R. R. v. Cal., 162 U. S. 91.

regard to what part thereof is employed within the State, or the amount of business done there. Even as applied to corporations engaged in interstate commerce such a tax is purely a franchise tax, and is not to be regarded as a tax upon interstate commerce.[39] With regard to a State tax upon the franchise of a bridge company, the late Mr. Chief Justice Fuller explained the foregoing principle as follows:

"Clearly the tax was not a tax on the interstate business carried on over or by means of the bridge, because the bridge company did not transact such business. That business was carried on by the persons and corporations which paid the bridge company tolls for the privilege of using the bridge. The fact that the tax in question was to some extent affected by the amount of the tolls received and, therefore, might be supposed to increase the rate of tolls, is too remote and incidental to make it a tax on the business transacted."[40]

The payment of such a tax, however, as we have previously seen, cannot be made a condition precedent to the right of a foreign corporation to engage in commerce within the State; the State must be satisfied to collect the tax in the ordinary manner, without the power to demand payment in advance for the privilege.[41]

Method of Determining Amount Of. In this connection it is proper to note that in fixing this franchise tax, a State may adopt the gross receipts of the business done as a method of measurement, even though these receipts are from interstate commerce. By a Maine statute every corporation or other person operating a railroad in the State was required to pay "an annual excise tax for the privilege of exercising its franchises" in the State. The gross annual transportation receipts were to be divided by the total number of miles operated, to get the average gross receipts per mile, and the tax was fixed with reference to

[39] Horn Silver Mining Co. v. New York State, 143 U. S. 305; Postal Tel Co. v. Adams, 155 U. S. 688.

[40] Henderson Bridge Co. v. Ky., 166 U. S. 150, 153.

[41] Postal Tel. Co. v. Adams, 155 U. S. 688.

these. In the case of a railroad partly within and partly without the State, or operated as part of a line extending beyond the State, the tax was ascertained in the same way, but was assessed for the number of miles operated within the State, that is, the gross receipts per mile was multiplied by the number of miles operated within the State. In the opinion of the majority of the Supreme Court, this resort to the receipts was not a tax on the receipts, and there was no interference with transportation, and no invalid regulation of transportation.[42] But a State tax imposed directly upon the gross receipts of a railway is void as an interference with interstate commerce in so far as such receipts are derived from interstate business.[43]

§ 30. **Tax on Gross Receipts Void.** At first the Supreme Court held that taxes upon gross receipts derived from both interstate and intrastate traffic were valid, justifying the particular law considered upon the ground that as the tax was collectible only once every six months, the fund so taxed must have become mingled with the other property of the company and had lost the protection of its partial interstate origin.[44] Later, however, this decision was overruled, and the court held that gross receipts, as such, derived from interstate commerce were not subject to State taxation.[45] The foregoing rule does not mean, however, that a State may not tax the receipts of an interstate corporation where the tax is strictly confined to the intrastate business, and in no way relates to the interstate business of the company. Nor, as pointed out in the preceding section, does it forbid reference to the gross receipts for the purpose of ascertaining the State tax on the privilege of exercising franchise within the State, or determining the value of tangible property used therein.[46]

[42] Maine v. Grand Trunk R. R., 142 U. S. 217.

[43] Phila. S. S. Co. v. Pa., 122 U. S. 326; Lehigh Valley R. R. v. Pa., 145 U. S. 192; Me. v. Grand Trunk R. R., 142 U. S. 217.

[44] State Tax on Railway Gross Receipts, 15 Wall. 284.

[45] Phila. S. S. Co. v. Pa., 122 U. S. 326; Fargo v. Michigan, 121 U. S. 230.

[46] Me. v. Grand Trunk R. R., 142 U. S. 217; Pacific Express Co. v. Seibert, 142 U. S. 339; Lehigh Valley R. R. v. Pa., 145 U. S. 192.

§ 31. Tonnage Clause. By Article I, section 10, of the Constitution, it is provided in part, that "no State shall, without the consent of Congress, lay any duty of tonnage." While this clause undoubtedly affects commerce to a certain extent, nevertheless, in the words of Mr. Chief Justice Marshall:

"A duty of tonnage being part of the power of imposing taxes, its prohibition may certainly be made to depend upon Congress, without affording any implication respecting a power to regulate commerce."

The thing prohibited to the States is taxation proportioned to tonnage, say one dollar a ton, imposed upon a vessel "as an instrument of commerce, for entering or leaving a port, or navigating the public waters of the country."[47] This does not prevent taxation levied by a State upon the assessed valuation of ships at their *situs*,[48] so long as the tax is levied with regard to the value of the property, and not on the basis of their cubical contents as instruments of commerce.[49] If the fee is not really a tax, but merely compensation for the benefit of specific improvements or services, such as wharfage, quarantine inspection, and the like, it is unobjectionable, even though the charge be graduated according to tonnage. "The prohibition to the State against the imposition of a duty of tonnage was designed to guard against local hindrances to trade and carriage by vessels, not to relieve them from liability to claims for assistance rendered and facilities furnished for trade and commerce."[50] A charge for municipal wharfage may, therefore, be proportioned to the tonnage of vessels availing themselves of the privilege; wharfage is not tonnage. "A duty of tonnage is a charge for the privilege of entering, or trading, or lying in, a port or harbor; wharfage is a charge for the use of a wharf."[51] If the tax pro-

[47] Huse v. Glover, 119 U. S. 543, 549.
[48] Wheeling Transp. Co. v. Wheeling, 99 U. S. 273.
[49] State Tonnage Tax Cases, 12 Wall. 204.
[50] Keokuk Northern Line Packet Co. v. Keokuk, 95 U. S. 80, 84.
[51] Parkersburg Transp Co. v. Parkersburg, 107 U. S. 691, 696.

portioned as to tonnage is imposed on every vessel arriving at quarantine station irrespective of whether any service is rendered or not, then it is bad as a tonnage tax, even though its proceeds are intended to defray the expense of quarantine regulations.[52]

[52] Peete v. Morgan, 19 Wall. 581.

CHAPTER V

CONGRESS AND ADMIRALTY JURISDICTION

§ 32. Regulating Navigation. As incidental to the power to regulate commerce, particularly foreign commerce, Congress, as we have seen, has power to regulate navigation as one of the principal instrumentalities of commerce, and to prescribe the rules necessary to promote the safety and convenience of navigable waters.[1] So far as the commerce clause is concerned, Congress has no power over the internal navigation of a State. For that power, if it exists at all, we must look to another section of the Constitution.

By Article III, section 2, it is provided that the Federal judicial power shall extend to all cases of admiralty and maritime jurisdiction. Note that this clause purports to pertain to the Federal judiciary alone, and contains no express grant of power to the Federal legislature. Yet under this clause, in addition to the power granted by the commerce clause, Congress has been held to have power over maritime affairs, and to be authorized to regulate the navigable waters of the United States.[2] In this respect Congress has greater power than that granted by the commerce clause alone, for the latter does not relate to the purely internal commerce of a State, while matters connected with the navigation of the navigable waters of the United States are within the maritime jurisdiction even though the commerce involved be purely internal, or even though no commerce at all is involved.[3]

Navigable Waters of the United States. The admiralty jurisdiction extends to all navigable waters of the United States.[4] Under the English admiralty law, navigable wa-

[1] Leovy v. U. S., 177 U. S. 621.
[2] *In re* Garnett, 141 U. S. 1.
[3] *Idem*, footnote 2.
[4] The Daniel Ball, 10 Wall. 557, 563.

ters meant such waters as were subject to the ebb and flow of the tide. The definition, however, was found too narrow for the United States with its great rivers and large bodies of inland waters. Accordingly, the term navigable waters of the United States, in contradistinction from the navigable waters of the States, includes such waters as "form in their ordinary condition by themselves, or by uniting with other waters, a continued highway over which commerce is or may be carried on with other States or foreign countries in the customary modes in which such commerce is conducted by water."[5] Navigability alone is not the sole test; waters to be navigable, in order to be within both the maritime power and the incidental power under the commerce clause, must be accessible from another State or country.[6] Great Salt Lake is navigable, but is not within the Federal admiralty jurisdiction, because inaccessible by waters from any other State than Utah. On the other hand, though a river connects with waters of other States, it may be so obstructed as to be inaccessible to navigation from other States, and so not within the maritime power. But if water be both navigable and accessible, it will be within the maritime power, even though artificial water like the Erie Canal.[7]

As to the relative power of Congress and the States over navigable waters, the general rules elsewhere mentioned apply. Congress may, if it chooses, occupy the whole field of regulation, may authorize the erection of bridges, wharves, and piers, the construction of canals and dams, may regulate shipping, pilotage and ferries.[8] On the other hand, the States, so long as there is no direct burden on interstate or foreign commerce, and so long as the free navigation of the waters is not impaired, may impose local and police regulations thereon, if there is no national legislation to

[5] The Daniel Ball, 10 Wall. 557, 563; Miller v. N. Y., 109 U. S. 385; Escanaba v. Chi., 107 U. S. 678; Nelson v. Leland, 22 How. 48.

[6] Commonwealth v. King, 150 Mass. 221.

[7] The Robt. W. Parsons, 191 U. S. 17.

[8] S. Carr v. Georgia, 93 U. S. 4; Gilman v. Phila., 3 Wall. 713; Leovy v. U. S., 177 U. S. 621; Miller v. N. Y., 109 U. S. 385.

forbid.[9] For instance, in order to improve its lands and the health of its people, a State may, in the exercise of its police power, with the consent of Congress, authorize the construction of dams across its interior streams;[10] and dams so constructed—even across navigable waters and tidewater creeks—may be freely regulated until Congress interferes and either assumes control of the improvements or compels their removal.[11] Further, the interference of Congress and the exclusion of State action over State waters must be express, and not by mere implication.[12]

[9] Sands v. Manistee River Imp. Co., 123 U. S. 288; Huse v. Glover, 119 U. S. 543; Veazie v. Moor, 14 How. 568.

[10] Manigault v. Springs, 199 U. S. 473.

[11] U. S. v. Billingham Boom Co., 176 U. S. 211; Huse v. Glover, 119 U. S. 543.

[12] Cummings v. Chi., 188 U. S. 410.

PART IV

ANTI-TRUST LEGISLATION AND LITIGATION*

Twenty-one years ago Congress passed the so-called "Sherman Anti-Trust Law." This designation is a misnomer. The law as it stands is not attributable to Senator Sherman, nor is the law properly called an "anti-trust law." Senator Hoar says in his Autobiography that this law is called the Sherman Act "for no other reason that I can think of except that Mr. Sherman had nothing to do with framing it whatever" (Vol. II, p. 363).

The word trust acquired an unenviable prominence in the eighties and became the familiar and common expression for a combination of competing interests under one management. Today, the so-called trust in its original sense has become rare, but the expression survives and has assumed a generic significance as indicating and connoting every form of combination of competing interests. The original trust was an arrangement whereby a number of competing manufacturers, individual or corporate, while retaining their individual or corporate identity and their individual or corporate ownership of their respective properties, put into the hands of trustees their respective interests, the trustees being clothed with the right to dictate to the respective competitors the terms on which they should compete, the amount and character of their output, and the prices at which the output should be sold. The large combinations of capital which now exist in various

**Address by William B. Hornblower, LL.D. Reprinted from Proceedings of American Bar Association.*

branches of industry have inherited the opprobrium attaching to this term. To call a combination or a corporation a trust is to excite public condemnation and to put the combination on the defensive.

The statute passed in 1890 by Congress is entitled, "An Act to Protect Trade and Commerce against Unlawful Restraints and Monopolies." We still for purposes of convenience continue to call the law the Sherman Anti-Trust Law, although it is not the Sherman Law as originally reported by the Finance Committee of the Senate of which Senator Sherman was chairman and although it is not particularly directed against trusts, it is directed generally against contracts or combinations or conspiracies in restraint of trade and also against monopolizing.

This law was carefully framed, amended, and re-amended and was debated in detail by the ablest lawyers in Congress, some of the ablest lawyers who ever sat in that body, including such men as Senators Edmunds, of Vermont, and George F. Hoar, of Massachusetts. One would have supposed that if ever a statute would prove to be unambiguous, intelligible and enforceable, this would be that statute; yet it is safe to say that no statute ever passed since the foundation of the government has been the subject of more difference of opinion or the cause of more perplexity, both to judges and lawyers, than this same statute. Three times have the justices of the United States Supreme Court been divided in opinion on the question of its construction; twice by a vote of five to four and once by a vote of five to three.

In its latest phase, the question of construction has been the occasion for a most violent and impassioned dissent by the senior justice of the court from the views expressed by the Chief Justice, concurred in by all the associate justices, except the senior justice, who in his dissenting opinion has accused his brethren of judicial legislation and of practically nullifying the will of Congress as expressed in the statute and of reversing their previous decisions.

The reason why the eminent and able lawyers who framed this statute failed in their attempt to enact a law which

should be clear and unambiguous, is a reason which inheres in all attempts to provide for a large class of cases by statutory enactment. The principles of the common law grow by a process of organic growth. The law slowly develops and enlarges to meet actual cases and existing situations. The law is made by applying principles of morality and public policy and sound reason to a given state of facts. On the other hand, law-making by legislation must undertake to deal with a vast number of complicated situations thereafter to arise, and must deal with such situations either by very general phraseology which will be dangerous when applied to all possible cases coming within the apparent meaning of the language or else it must go into great detail and deal with the subject-matter in its various phases.

With regard to the subject-matter attempted to be covered by the Sherman Law, there were peculiar difficulties and dangers. As I have pointed out on a prior occasion, the requisites of a proper statute are:

(1) That its language should be capable of application to all cases covered by such language construed in its ordinary and natural sense;
(2) That it should be applicable to all persons and corporations coming within its terms without arbitrary discrimination;
(3) That it should be clear and certain in its provisions so that all persons can be guided thereby.

This statute fails to comply with any one of these requisites. The first section of the act provides that "every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce among the several States or with foreign nations, is hereby declared to be illegal."

The phrase contracts "in restraint of trade", as used in the common-law decisions, primarily had reference to contracts by which a merchant or manufacturer agreed to sell to a competitor in the same line of business the good will of his business, such sale to be accompanied by a covenant on the part of the vendor to refrain from competition.

Such contracts were originally held to be void as against public policy because necessarily restraining trade. The leading case on this subject is Mitchel v. Reynolds, 1 P. Wms. 181. Gradually, however, such contracts came to be recognized as valid in cases where the covenant to refrain from competition was limited in time and space so as to be not an unreasonable restriction or as the courts sometimes stated it, a restriction no greater than was necessary in order to protect the vendee in the right to the use of the property purchased by him, or as it was otherwise put, a contract "in partial restraint of trade" as distinguished from a contract "in general restraint of trade." It was with regard to such contracts that the words *reasonable* and *unreasonable* came to be used and contracts in reasonable restraint of trade, were sustained by the courts, while contracts which were in unreasonable restraint of trade were condemned by the courts. The test of what is a reasonable or an unreasonable restraint of trade has been gradually liberalized by the courts from time to time until now, as laid down by the Court of Appeals of New York in the Diamond Match Case (106 N. Y. 473), and by the House of Lords in England in the Nordenfelt Case (L. R. (1894) Appeal Cases, 535), a covenant by a vendor to refrain from competition is valid even though practically unrestricted as to time and space, provided it is necessary for the protection of the vendee that an unrestricted covenant should be made.

There were, however, other classes of contracts which came within the condemnation of the common law as "in restraint of trade", such as contracts between competitors to regulate prices or to prevent competition among themselves or by rivals. These classes of contracts were held to be illegal as tending to raise prices or to create a monopoly by limiting competition. These classes of contracts were evidently intended to be covered by the statute.

Manifestly, however, if the statute were to be construed literally as declaring "every" contract in restraint of trade to be illegal and if that phrase were to be construed as

meaning that every contract which *actually* restrains trade or competition shall be illegal, not only would it run counter to the common law, but it would be practically meaningless and unenforceable. This is clearly pointed out by Judge Lacombe in striking and telling example of a contract between "two individuals who have been driving rival express wagons between villages in two contiguous States, who enter into combination to join forces and operate a single line." As Judge Lacombe well points out, such combination operates to "restrain an existing competition" (164 Fed. Rep. 702). This of course amounts to a *reductio ad absurdum,* the only escape from which is to say, as has been said by some of the defenders of the literal construction of the law, that the law was not designed and will not be interpreted by the courts to apply to trifles. The suppression, however, of competition between two rival expressmen may be as important to a small community as the suppression of competition between two great railroad systems is to a large community.

The objections to Section 1 of this act were emphatically pointed out by no less a person than President Roosevelt. In his annual message to Congress under date of December 8, 1908, he said:

"I believe that it is *worse than folly* to attempt to prohibit *all* combinations as is done by the Sherman Anti-Trust Law, because such a law can be enforced only *imperfectly* and *unequally,* and its enforcement works almost as much hardship as good."

The second section of the act—with regard to "monopolizing," is equally incapable of a literal interpretation or a literal enforcement. This section reads: "Every person who shall monopolize, or *attempt to monopolize,* or combine or conspire with any other person or persons to monopolize, *any part* of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor."

The absurdity of this section if literally construed and

enforced is well pointed out by Judge Ward in his dissenting opinion in the Tobacco Case in the U. S. Circuit Court (164 Fed. Rep. 727):

"As this section prohibits a monopoly of or an attempt to monopolize any *part* of such commerce, it cannot be literally construed. So applied, the act would prohibit commerce altogether."

The same criticism is forcibly made by Judge Sanborn in delivering the opinion of the court in Whitwell v. The Continental Tobacco Co., 125 Fed. Rep. 454:

"But is every attempt to monopolize any *part* of interstate commerce made unlawful and punishable by Section 2 of the Act of July 2, 1890, C. 647, 26 Stat. 209? If so, no interstate commerce has ever been lawfully conducted since that act became a law, because every sale and every transportation of an article which is the subject of interstate commerce is a successful attempt to monopolize that part of this commerce which concerns that sale or transportation. An attempt by each competitor to monopolize a part of interstate commerce is the very root of all competition therein. Eradicate it, and competition necessarily ceases—dies. Every person engaged in interstate commerce necessarily attempts to draw to himself, and to exclude others from, a part of that trade; and, if he may not do this, he may not compete with his rivals, and all other persons and corporations must cease to secure for themselves any part of the commerce among the states, and some single corporation or person must be permitted to receive and control it all in one huge monopoly."

In fact this statute never has been and never can be literally and strictly applied. To so apply it would produce chaos in the business world. The statute must be applied not according to its language, but according to its reasonable meaning or else it becomes the instrument, not of regulation, but of injustice and of ruin to the mercantile community.

The phrase "restraint of trade" as used by the courts is, as I understand the cases, the equivalent of restraint

of competition, that is to say, if free competition be restrained, trade is restrained. It has been claimed with great insistence that there is a distinction between "restraint of trade" and "restraint of competition", and that the latter is not unlawful except as it results in the former, and if the restraint of competition does not in fact restrain the volume or extent of trade, there is no illegal restraint of trade, and it is further insisted that this distinction has been recognized by the Supreme Court in its recent opinions in the Standard Oil and Tobacco cases. With all due respect for the ability of those who support these views, I am unable to concur in their conclusions.

The common-law meaning of "restraint of trade" was certainly "restraint of competition." The numerous cases in the common-law courts discussing the validity or invalidity of contracts in restraint of trade turn on the question of whether they reasonably or unreasonably interfere with free competition. As is said in the head-note to the opinion of Mr. Justice Harlan in the Northern Securities Case, 193 U. S. 198: "The Anti-Trust Act has prescribed the rule of *free competition.*" . . . "The natural effect of competition is to increase commerce, and an agreement whose direct effect is to prevent this play of *competition* restrains instead of promotes trade and commerce."

It is because the agreements in the *Addyston Pipe* Case (175 U. S. 211), the *Montague* Case (193 U. S. 38), and the *Swift* Case (196 U. S. 38) *restrained competition* that they were held to be in *restraint of trade,* and finally, in the *Standard Oil* Case and the *Tobacco* Case, it is because the combinations in these cases were held to unduly restrain free competition that they were held to be in *undue restraint of trade.*

It is said by Mr. Chief Justice White in the recent Standard Oil Case, speaking of the common-law decisions:

"It is also true that while the principles concerning contracts in restraint of trade, that is, voluntary restraint put by a person on his right to pursue his calling, hence only operating subjectively, came generally to be recog-

nized in accordance with the English rule, it came moreover to pass that contracts or acts which it was considered had a monopolistic tendency, especially those which were thought to *unduly diminish competition* and hence to enhance prices—in other words, to monopolize—came also in a generic sense, to be spoken of and treated, as they had been in England, as restricting the due course of trade, and therefore as being in restraint of trade."

And again:

"The dread of enhancement of prices and of other wrongs which it was thought would flow from the *undue limitation of competitive conditions* caused by contracts or other acts of individuals or corporations, led, as a matter of public policy, to the prohibition or treating as illegal all contracts or acts which were unreasonably *restrictive of competitive conditions,* either from the nature or character of the contract or act or where the surrounding circumstances were such as to justify the conclusion that they had not been entered into or performed with the legitimate purpose of reasonably forwarding personal interest and developing trade, but on the contrary were of such a character as to give rise to the inference or presumption that they had been entered into or done with the intent to do wrong to the general public and to limit the right of individuals, thus restraining the free flow of commerce and tending to bring about the evils, such as enhancement of prices, which were considered to be against public policy."

In stating the conclusions of the court, the Chief Justice says:

"In view of the common law and the law in this country as to the restraint of trade, which we have reviewed, and the illuminating effect which that history must have under the rule to which we have referred, we think it results: (a) That the context manifests that the statute was drawn in the light of the existing practical conception of the law of restraint of trade, because it groups as within that class, not only contracts which were in restraint of trade in the subjective sense, but all contracts or acts which theoretically were attempts to monopolize, yet which in practice had come to be considered as in restraint of trade in a broad sense."

In the Tobacco Case, there was no proof that the volume of trade had been in fact restrained. On the contrary, the proof showed an enormous increase of the volume of trade and a large increase in the number of independent dealers during the existence of the American Tobacco Company, but the court held that there was an intent to restrict or suppress competition and to form a monopoly which rendered the combination obnoxious to the statute as a combination "in restraint of trade."

As one of the counsel who argued the Tobacco Case before the Supreme Court, appearing in that court in behalf of the Imperial Tobacco Company of Great Britain and Ireland, I ought to say in justice to myself and in justice to my client, so far as it was involved in the conclusion arrived at by the court, and in justice to the American Tobacco Company, that I did not regard and do not now regard the testimony as justifying the sweeping condemnation announced by the court on the facts, or the decision arrived at by the court, even as to the American Company, much less as to the Imperial Company. I concur, however, fully in the views expressed by the court as to the construction of the statute, as I shall hereafter more fully point out.

Taking it as established that "restraint of trade" means restraint of competition, the necessity of a reasonable construction of the statute is clearly apparent.

While the maxim that "competition is the life of trade" is in a certain sense a correct proposition, yet there is a point at which competition becomes the death of trade. It may well be that two competitors, carrying on business in competition with each other, may engage in such ruinous competition by cutting prices or otherwise that one or the other must necessarily be driven to the wall. Unless therefore one or both of those competitors can protect himself or themselves by a mutual agreement involving the sale of the property of one to the other, or by a combination to regulate prices, one or the other must be forced to the wall and thus practical monopoly will result. Undue competition may thus lead to monopoly while a reasonable regulation

or a reasonable arrangement between the competitors may prevent monopoly. A rigid and drastic statute overreaches itself, while a reasonable and just statute, which is readily enforceable, will accomplish beneficial results. Prohibition of all combinations and of all restraint of trade is unwise. Civilization means co-operation; co-operation means combination; combination means restraint of competition.

There has been so much misunderstanding and so much intentional or unintentional misrepresentation of the recent opinions of the U. S. Supreme Court in the Standard Oil and the Tobacco Cases and so much unjust and unfounded criticism of those opinions as an alleged departure from and repudiation of the previous decisions of the court, that a brief review of the decisions is necessary to a clear understanding of the situation.

The extremists have opened the vials of their wrath upon the court, and sarcasm, abuse and even threats have been freely indulged in by those who inveigh against what they call judicial legislation.

Let us endeavor to consider the history of the litigation calmly and dispassionately and see how far the critics are justified in their attacks on the court. I shall not hope to satisfy the radical who "sees red" or the pessimist who "thinks blue"; but I shall hope to convince the calm intelligence of the American Bar Association that there never was a more uncalled for, unwarranted, or unjustified attack upon a judicial opinion.

In this review of the decisions, it is well to bear in mind what is said by Senator Hoar (Autobiography, Vol. II, p. 364), as to what was intended by its framers:

"It was expected that the court, in administering that law, would confine its operation to cases which are contrary to the policy of the law, treating the words 'agreements in restraint of trade' as having a technical meaning, such as they are supposed to have in England. The Supreme Court of the United States went in this particular farther than was expected. In one case it held that

'the bill comprehended every scheme that might be devised to restrain trade or commerce among the several States or with foreign nations.' From this opinion several of the court, including Mr. Justice Gray, dissented. It has not been carried to its full extent since, and I think will never be held to prohibit the lawful and harmless combinations which have been permitted in this country and in England without complaint, like contracts of partnership, which are usually considered harmless. We thought it was best to use this general phrase which, as we thought, had an accepted and well-known meaning in the English law, and then after it had been construed by the court, and a body of decisions had grown up under the law, Congress would be able to make such further amendments as might be found by experience necessary."

The first great legal battle over the meaning and application of the statute took place within two or three years after its enactment and was an attempt to deal with the so-called Sugar Trust and to put an end to a great and growing power of control over one of the necessaries of life. The attempt, however, to reach the Sugar Trust was a failure. The Supreme Court held in the Knight Case (156 U. S. 1), that the statute was not intended to "assert the power to deal with monopoly directly as such; or to limit or restrict the right of corporations created by the States or the citizens of the States in the acquisition, control, or disposition of property; or to regulate or prescribe the price or prices at which such property, or the products thereof, should be sold; or to make criminal the acts of persons in the acquisition and control of property which the States of their residence or creation sanctioned or permitted." The bill in the Knight Case seems to have been drawn in such shape as to fail to sufficiently disclose that the Sugar Trust was actually carrying on the business of interstate trade or commerce in the *manufactured product.*

The next great legal battle took place in the Trans-Missouri Case and the Joint Traffic Case, both of which were instituted within two or three years after the passage of the act. It might reasonably have been expected that

these cases would settle once and for all what the statute meant and what were its applications and its limitations. Unfortunately the decisions in these cases were but starting points for new uncertainties and furnished *obiter dicta* which have misled the Bench and the Bar in subsequent cases and which remained until 1911 the source of new perplexities. Both of these cases were decided by a bare majority of the court.

The prevailing opinion in the Trans-Missouri Case contained *dicta* which were understood to mean that every contract which operated in restraint of trade was invalid under the statute whether such contract was reasonable or unreasonable. The main ground of contention in that case was whether the Sherman Law applied to railroad companies engaged in interstate transportation so far as to prohibit mutual regulation by agreement of rates for transportation. The majority of the court held that it did, the minority of the court dissenting on this proposition. Incidentally the majority opinion as delivered by Mr. Justice Peckham announced the proposition that the Sherman Law applies to all combinations in restraint of interstate or foreign trade or commerce without exception or limitation and that the prohibitions of that section are not confined to unreasonable restraints of such trade or commerce, Mr. Justice Peckham saying in his opinion:

"It is now with much amplification of argument urged that the statute in declaring illegal every combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce, does not mean what the language used therein plainly imports, but that it only means to declare illegal any such contract which is in unreasonable restraint of trade while leaving all others unaffected by the provisions of the act; that the common law meaning of the term "contract in restraint of trade' includes only such contracts as are in unreasonable restraint of trade, and when that term is used in the Federal statute it is not intended to include all contracts in restraint of trade, but only those which are in unreasonable restraint thereof. The term is not of such limited significance."

United States v. Freight Ass'n (166 U. S. 327).

It was most unfortunate that the learned justice who delivered the opinion of the court used this language which was really an *obiter dictum.* All that was really decided by the court in that case was that a contract to regulate rates made between railroad companies carrying on a public service business as common carriers, exercising public franchises, was against public policy as in restraint of trade and came within the prohibition of the Sherman Law irrespective of the question of whether the rates prescribed were reasonable or unreasonable, or whether the agreement would operate beneficially or injuriously. The circumstance that the combination between the railroad companies was capable of being operated so as to prescribe unjust or unreasonable rates was held to be sufficient to bring it within the intent of the statute, notwithstanding the fact that the actual operation of the combination was beneficial to the community.

Mr. Justice Peckham, however, followed up his *obiter dictum* by a very emphatic statement which he subsequently enlarged upon in the Joint Traffic Case and by which he carefully warned against the very construction which was subsequently placed upon these decisions by the profession and by some of the lower courts, and even by the Supreme Court itself in subsequent cases. Thus, in the opinion of Mr. Justice Peckham as delivered in the Joint Traffic Case (171 U. S. 566), he says:

"We also repeat what is said in the case above cited that 'the act of Congress must have a *reasonable construction* or else there would scarcely be an agreement or contract among business men that could not be said to have indirectly or remotely some bearing upon interstate commerce and possibly to restrain it.' To suppose, as is assumed by counsel, that the effect of the decision in the Trans-Missouri Case is to render illegal most business contracts or combinations, however indispensable and necessary they may be, because as they assert, they all restrain trade in some remote and indirect degree, is to make a most violent assumption, and one not called for or jus-

tified by the decision mentioned, or by any other decision of this court."

Mr. Justice Peckham further says:

"In dwelling upon the far-reaching nature of the language used in the act as construed in the case mentioned, counsel contend that the extent to which it limits the freedom and destroys the property of the individual can scarcely be exaggerated, and that ordinary contracts and combinations, which are at the same time most indispensable, have the effect of somewhat restraining trade and commerce, although to a very slight extent, but yet, under the construction adopted, they are illegal.

"As examples of the kinds of contracts which are rendered illegal by this construction of the act, the learned counsel suggest all organizations of mechanics engaged in the same business for the purpose of limiting the number of persons employed in the business, or of maintaining wages; the formation of a corporation to carry on any particular line of business by those already engaged therein; a contract of partnership or of employment between two persons previously engaged in the same line of business; the appointment by two producers of the same person to sell their goods on commission; the purchase by one wholesale merchant of the product of two producers; the lease or purchase by a farmer, manufacturer, or merchant of an additional farm, manufactory, or shop; the withdrawal from business of any farmer, merchant, or manufacturer; a sale of the good will of a business with an agreement not to destroy its value by engaging in a similar business; and a covenant in a deed restricting the use of real estate. It is added that the effect of most business contracts or combinations is to restrain trade in some degree.

"This makes quite a formidable list. It will be observed, however, that no contract of the nature above described is now before the court, and there is some embarrassment in assuming to decide herein just how far the act goes in the direction claimed. Nevertheless, we might say that the formation of corporations for business or manufacturing purposes has never, to our knowledge, been regarded in the nature of a contract in restraint of trade or commerce. The same may be said of the contract of partnership. It might also be difficult to show that the appoint-

ment by two or more producers of the same person to sell their goods on commission was a matter in any degree in restraint of trade.

"We are not aware that it has ever been claimed that a lease or purchase by a farmer, manufacturer, or merchant of an additional farm, manufactory, or shop, or the withdrawal from business of any farmer, merchant, or manufacturer, restrained commerce or trade within any legal definition of that term; and the sale of a good will of a business with an accompanying agreement not to engage in a similar business was instanced in the Trans-Missouri Case as a contract not within the meaning of the act; and it was said that such a contract was collateral to the main contract of sale and was entered into for the purpose of enhancing the price at which the vender sells his business."

Mr. Justice Peckham further states the real point decided and the only point decided as follows (171 U. S. 568):

"*The question really before us is* whether Congress, in the exercise of its right to regulate commerce among the several States, or otherwise, has the power to prohibit, as in restraint of interstate commerce, *a contract or combination between competing railroad corporations* entered into and formed for the purpose of establishing and maintaining interstate rates and fares for the transportation of freight and passengers on any of the railroads parties to the contract or combination, *even though the rates and fares thus established are reasonable.* Such an agreement directly affects and of course is intended to affect the cost of transportation of commodities, and commerce consists, among other things, of the transportation of commodities, and if such transportation be between States it is interstate commerce. . . .

"Has not Congress with regard to interstate commerce and in the course of regulating it, *in the case of railroad corporations,* the power to say that no contract or combination shall be legal which shall restrain trade and commerce by shutting out the operation of the general law of competition? We think it has."

The learned Justice proceeds to discuss at length the nature of the franchises of a railroad, and on page 570 says:

"We do not think, when the grantees of this public franchise are *competing railroads* seeking the business of transportation of men and goods from one State to another, that ordinary freedom of contract in the use and management of their property requires the right to combine as one consolidated and powerful association for the purpose of stifling competition among themselves, and of thus keeping their rates and charges higher than they might otherwise be under the laws of competition. And this is so, even though the *rates* provided for in the agreement may for the time be not more than are *reasonable.* They may easily and at any time be increased. It is the *combination of these large and powerful corporations* covering vast sections of territory and influencing trade throughout the whole extent thereof, and acting as one body in all the matters over which the combination extends, that constitutes the alleged evil, and in regard to which, so far as the combination operates upon and restrains interstate commerce, Congress has power to legislate and to prohibit."

In view of these carefully measured statements of Mr. Justice Peckham in the Trans-Missouri Case and in the Joint Traffic Case, and in view of his express statement that "the act is to have a reasonable construction", it is difficult to understand the criticism that has been made upon the language of Mr. Chief Justice White in the recent decisions in the Standard Oil and Tobacco Cases, to the effect that the statute is to be interpreted by the "light of reason".

Furthermore, in the case of the *Northern Securities Company,* 193 U. S. 197, which, as will be remembered, was a case dealing with the question of restraining trade and commerce between competing railroads, by the device of a holding company, holding a majority of the stock of the two competing companies, the court divided five to four on the question of the illegality of such a holding company, but Mr. Justice Brewer took occasion to say, in concurring with the majority, that he wished to modify his concurrence in the opinion of Mr. Justice Peckham in the Trans-Missouri Case, so far as that opinion stated that "every" contract or combination in restraint of trade was within the statute, whether "reasonable or unreasonable." As Mr. Justice

Brewer was one of the five justices whose concurrence made up the majority necessary to a decision in the Trans-Missouri Case, his expression of opinion in the Northern Securities Case made the unfortunate *obiter dictum* of Mr. Justice Peckham the *dictum* of a *minority* instead of a majority of the court and deprived it of any binding authority in subsequent cases.

Mr. Justice Brewer, in his opinion in the Northern Securities Case, said (193 U. S. 361):

"I think that in some respects the reasons given for the judgments cannot be sustained. Instead of holding that the Anti-Trust Act included all contracts, reasonable or unreasonable, in restraint of interstate trade, the ruling should have been that the contracts there presented were unreasonable restrains of interstate trade, and as such within the scope of the act. That act, as appears from its title, was leveled at only unlawful restraints and monopolies.

"Congress did not intend to reach and destroy those minor contracts in partial restraint of trade which the long course of decisions at common law had affirmed were *reasonable* and fit to be upheld. The purpose rather was to place a statutory prohibition with prescribed penalties and remedies upon those contracts which were in direct restraint of trade, *unreasonable* and against public policy. Whenever a departure from common-law rules and definitions is claimed, the purpose to make the departure should be clearly shown. Such a purpose does not appear and such a departure was not intended."

He further says (at p. 364):

"I have felt constrained to make these observations for fear that the broad and sweeping language of the opinion of the court might tend to unsettle legitimate business enterprises, stifle or retard wholesome business activities, encourage improper disregard of reasonable contracts and invite unnecessary litigation."

In view of these emphatic statements of Mr. Justice Brewer, one of the majority in the Trans-Missouri Case, in

which he expressly repudiates the "reasonable or unreasonable" *dictum,* it is difficult to understand how any one can assert that that *dictum* is binding in subsequent cases on the principle of *stare decisis,* or that to call that *dictum* in question is sacrilege.

The situation after the Northern Securities Case was thus forcibly put by the Hon. Simeon E. Baldwin, the present Governor of Connecticut, at the time Chief Justice of that State, in 1904, in his work on "American Railroad Law," on page 16 of the first edition, in a footnote:

"That the phrase 'agreements in restraint of trade' was adopted by the framers of the Sherman Act, supposing that it would be given the same construction accepted by the English courts, see George F. Hoar's 'Autobiography,' II, 364. Mr. Justice Brewer, by whose concurrence in the judgment the decision mentioned in the preceding note (viz., the Northern Securities Co. Case) was reached, in his opinion approves such a construction as will make the act applicable only to unreasonable contracts and combinations which are in direct restraint of trade."

Judge Baldwin then adds:

"It seems probable that this will ultimately be the prevailing view."

A brief resumé will be needful of the other decisions of the Supreme Court intermediate between the Trans-Missouri and Joint Traffic Cases and the latest cases of the Standard Oil and the Tobacco Companies bearing on the interpretation and application of the Sherman Law to mercantile and manufacturing combinations and contracts.

Two cases decided at the same term of court as the Trans-Missouri and Joint Traffic Cases, U. S. v. Hopkins, 171 U. S. 579, and U. S. v. Anderson, 171 U. S. 604, were decided in favor of the defendants, the opinions in both of these cases being delivered by Mr. Justice Peckham—the same judge who had delivered the opinions in the Trans-Missouri and Joint Traffic Cases.

In the opinion in the Hopkins Case, Mr. Justice Peckham reiterates the statement that the statute must have a

"reasonable construction," and repeats what he had said in the Traffic Cases:

"The Act of Congress must have a reasonable construction or else there would scarcely be an agreement or contract among business men that could not be said to have, indirectly or remotely, some bearing upon interstate commerce, and possibly to restrain it" (171 U. S. 600).

The famous Addyston Pipe Case, 175 U. S. 211, involved an agreement between a number of rival and competing manufacturers to the effect that there should be *no competition* between them in certain States and territories. It was held that the *"direct, immediate and intended effect"* of the agreement was the *"enhancement" of the "price"*.

The agreement contemplated "fake" bids by the rival competitors and fixing the price at which one of the competitors could obtain the contract desired and below which none of the parties to the agreement was allowed to bid. The agreement would have been held to be against public policy and illegal at common law.

This Addyston contract was so flagrantly a violation not only of the letter, but of the spirit of the Sherman Act that it is difficult to conceive of any combination or conspiracy which could be brought within the act if that contract was held not to be within it.

In the very careful, able and elaborate opinion delivered by Judge Taft in this case in the U. S. Circuit Court of Appeals (85 Fed. Rep. 271), the authorities on "restraint of trade" at common law are exhaustively reviewed and the distinction is clearly pointed out between valid and invalid contracts "in restraint of trade".

At p. 282, Judge Taft says:

"In Horner v. Graves, 7 Bing. 735, Chief Justice Tindal, who seems to be regarded as the highest judicial authority on this branch of the law (see Lord Macnaghten's judgment in Nordenfelt v. Maxim Nordenfelt Co. [1894] App. Cas. 535, 567) used the following language: 'We do not see how a better test can be applied to the question whether

this is or not a *reasonable restraint of trade* than by considering whether the restraint is such only as to afford a fair protection to the interests of the party in favor of whom it is given, and not so large as to interfere with the interests of the public."

The case of Montague v. Lowry, 193 U. S. 38, was a case where there was a combination of wholesale dealers in tiles, mantels, and grates, who conspired to confine the business in California to the members of the combination, by *refusing to sell or deliver* tiles, grates or mantels to any other party in California and who conspired to *raise the prices* of those articles in the California market. The combination was one which would have been illegal at common law as against public policy.

The case of Swift & Co. v. U. S., 196 U. S. 375, involved *a combination of independent meat dealers,* who agreed not to *bid against each other* in the live stock markets, to *bid up prices for a few days* in order to induce shipments to the stock yards, to *fix selling prices* and to that end to *restrict shipments* of meat when necessary, to establish a uniform rule of credit to dealers, *and to keep a black list,* to make *uniform and improper charges for carriage, and to secure less than lawful freight rates to the exclusion of competitors.*

Assuming that that was a case of interstate commerce within the meaning of the Sherman Law, as was held by the court, it would be difficult to conceive of any element of a combination for unlawful restraint of trade or of an attempt to monopolize which was lacking in the Swift Case.

The case of Chattanooga Foundry v. Atlanta, 203 U. S. 390, was a sequel to the Addyston Pipe Case, the action being brought by the city of Atlanta against two of the members of the trust or combination which had been held unlawful in the Addyston Case. The only questions really discussed by the court in that case were as to the right of the city to maintain the action and as to the statute or limitations of Tennessee.

In the case of Shawnee Compress Company v. Anderson,

209 U. S. 423, an agreement of lease had been held by the Supreme Court of the territory of Oklahoma to be void as an unreasonable restraint of trade and as against public policy.

In the case the lessor company had agreed with the lessee company not only to go out of the field of competition and not to enter that field again, but had further agreed *"to render every assistance to prevent others from entering it."* There were other facts in the case showing that the lease was in aid of a scheme of monopoly on the part of the lessee company, the Gulf Compress Company. It was shown that the lessee company was in the business of leasing and operating competing compresses for the purpose of monopolizing as far as possible the business of compressing cotton in a large portion, if not all, of the cotton raising districts of the United States, and that the lease was procured from the Shawnee Company in pursuance of said scheme, and other leases of other compressors were also secured for like purposes "and that it is the design of the Gulf Compress Company to *increase the charge of compressing cotton."*

In the lease the Shawnee Company had agreed not only to refrain from competition, but to *"render the 'Gulf Company' every assistance in discouraging unreasonable and unnecessary competition."* It further appeared from the evidence that the Gulf Company had announced in a letter to the Shawnee Company in effect its purpose to create as far as possible a monopoly of the compressing business (page 433). It further appeared (page 434) that the "Gulf Company was a close corporation which, starting in Alabama, rapidly extended from Alabama to all the cotton growing territory."

The court recognized the principle announced in the Trans-Missouri and Joint Traffic Cases, "That the sale of the good will of a business with an accompanying agreement not to engage in a similar business was not a restraint of trade within the meaning of the Sherman Act." The court said:

"The principle is well understood. The restraint upon one of the parties must not be greater than protection to the other party requires, and it needs no further explanation than is given in Gibbs v. Baltimore Gas Co., 130 U. S. 396. The Supreme Court of the territory recognized the principle, but said: 'Tested by the general principles applicable to contracts of this character, *this agreement is far more extensive* in its outlook and more onerous in its intention *than is necessary to afford a fair protection to the lessee.*'"

The case of Continental Wallpaper Co. v. Voight Sons, 212 U. S. 227, was a case of an agreement between a number of manufacturers who organized a *selling company* through which their *entire output was sold to such persons only as would enter into a purchasing agreement by which their sales were restricted.* It was held that the clear effect of this arrangement was to restrain and monopolize. The agreement provided for selling to jobbers for the account of the Continental Wallpaper Company *at particular specified prices,* with particular discounts. The company was a selling company, organized *to control all the selling business* of the manufacturing wallpaper corporations, partnerships and persons who owned the stock of the Continental Wallpaper Company and who made separate contracts with that corporation giving it entire control of the selling business of the manufacturers. The illegality of this arrangement seemed to the court too clear for discussion, and was not in fact discussed by the court, the only question discussed and decided being whether a purchaser of goods at the stipulated prices could avoid payment on the ground that the vendor company was illegal combination.

In each and all of the cases which the court held to be obnoxious to the Sherman Act the contracts or combinations were clearly in "unreasonable" or "undue" restraint of trade, and would have been illegal at common law.

On the other hand, in Cincinnati Packet Company v. Bay, 200 U. S. 179, it is said by Mr. Justice Holmes at page 184, in upholding a covenant not to compete made in connection with a sale:

"It is argued, to be sure, that the last mentioned covenant is independent and not connected with the sale of the vessels. The contrary is manifested as a matter of good sense, and is proved even technically by the words 'it is also agreed as a part of the consideration of this agreement.' *By these words the covenant not to do business* between Cincinnati and Portsmouth for five years is *imported into the sale* of the ships, and made one of the conventional inducements of the purchase. *The price is paid not for the vessels alone, but for the vessels with the covenant.*

So, still more clearly, the parallel installments for five years are paid for the covenant, at least in part. It is said that there is no sale of good will. But the covenant makes the sale.

"Presumably all that there was to sell, beside certain instruments of competition, was the competition itself, and the purchasers did not want the vendors' names.

"This being our view of the covenant in question, whatever differences of opinion there may have been with regard to the scope of the Act of July 2, 1890, there has been *no intimation from any one,* we believe, *that such a contract, made as part of the sale of a business* and not as a device to control commerce, *would fall within the act.* On the contrary, it has been *suggested repeatedly* that *such a contract is not within the letter or spirit of the statute* (United States v. Trans-Missouri Freight Association, 166 U. S. 290, 329, United States v. Joint Traffic Association, 171 U. S. 505, 568), and it was so decided in the case of a patent, Bement v. National Harrow Co., 186 U. S. 70, 92. It would accomplish no public purpose, but simply would provide a loophole of escape to persons inclined to elude performance of their undertakings if the sale of a business and temporary withdrawal of the seller necessary in order to give the sale effect were to be declared illegal in every case where a nice scrutiny could discover that the covenant possibly might reach beyond the State line. We are of opinion that the agreement before us is not made illegal by either of the provisions thus far discussed."

Coming now to a consideration of the recent decisions of the Supreme Court in the Standard Oil Case and in the Tobacco Case, I submit that the opinions in these cases are in consonance with and not a repudiation of the previous

decisions of the court, so far as they distinguish between "reasonable" and "unreasonable" contracts.

In discussing these decisions I wish to once more point out, as I have already stated, that while I regard the opinions of the court, so far as they discuss the construction of the statute, as correct expositions of the meaning and intent of the statute, I do not wish to be understood as concurring in the conclusion of the court as to the facts of the case or as to the application of the statute to the American Tobacco Company or the Imperial Tobacco Company of Great Britain and Ireland, the latter of which companies I represented on the argument in the Supreme Court.

The opinions of Mr. Chief Justice White do not, in fact, use the word *unreasonable* in defining the class of contracts prohibited by the statute, but substitute for that word the word "*undue*" or "*unduly*". The Chief Justice would have been justified by the previous decisions of the courts in using the term "unreasonable". The test, however, as actually laid down by the Chief Justice in his opinions in those cases concurred in by all the justices except Mr. Justice Harlan, is that contracts are within the statute which *unduly* restrain trade.

It is quite true that this word apparently interjects into the statute a test which the statute itself does not apply. The statute says every contract in restraint of trade. The court says every contract in undue restraint of trade. By the insertion of this word undue or unduly, however, the statute is made logical, reasonable, and enforcible. It is quite true that the test of what is a due or an undue restraint of trade is left an open question which the court must decide in each case as it comes up, upon the facts and circumstances of that case, but the same is true of a vast number of other matters which are the subject of litigation. Where a hard and fast rule cannot be applied, then it is necessary that discretion should be allowed to the courts in determining between what is lawful and what is unlawful, what permissible and what not permissible.

Just what did the Supreme Court hold in the Standard Oil and Tobacco Cases? And just how would the law read if these opinions were set aside by legislation? Let us test the logic of those who criticize these opinions as judicial legislation by making them read as the critics would have them read.

In the Standard Oil opinion, Mr. Chief Justice White says that the statute "evidenced the intent not to restrain the right to make and enforce contracts, whether resulting from combination or otherwise, which did not *unduly* restrain interstate or foreign commerce, but to protect that commerce from being restrained by methods, whether old or new, which would constitute an interference that is an *undue restraint.*"

And again, the Chief Justice, referring to the second section of the act, which prohibits monopolizing, says: "The ambiguity, if any, is involved in determining what is intended by monopolize. But this ambiguity is readily dispelled in the light of the previous history of the law of restraint of trade to which we have referred and the indication which it gives of the practical evolution by which monopoly and the acts which produce the same result as monopoly, that is, an *undue restraint of the course of trade,* all came to be spoken of as, and to be indeed synonymous with, restraint of trade."

And again he says that the purpose of the statute "was to prevent *undue restraint* of every kind or nature."

And again, speaking of the remedies to be awarded by the court, he says: "The fact must not be overlooked that injury to the public by the prevention of an *undue* restraint on, or the monopolization of trade or commerce is *the foundation upon which the prohibitions of the statute rest,* and moreover that one of the fundamental purposes of the statute is to protect, not to destroy, rights of property."

In the Tobacco Case, the Chief Justice says: "It was held in the Standard Oil Case that as the words restraint of trade at common law and in the law of this country at

the time of the adoption of the Anti-Trust Act only embraced acts or contracts or agreements or combinations which operated to the prejudice of the public interests by *unduly restricting competition* or *unduly obstructing the due course of trade* or which, either because of their inherent nature or effect or because of the evident purpose of the acts, etc., *injuriously restrained trade,* that the words as used in the statute were designed to have and did have but a like significance."

Now, let us eliminate the word *unduly* and substitute *duly* and see how the statute would read: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce (even though it *duly* restrains such trade or commerce) among the several States or with foreign nations, is hereby declared to be illegal."

The absurdity of any such statutory declaration is manifest.

The Chief Justice applies the "rule of reason" to the statute and holds that the statute is to have a "reasonable construction", but in so doing, he simply follows the decision of the court in the Trans-Missouri Case and quotes the exact language of Mr. Justice Peckham in his opinion in that case.

Surely the most extreme champion of literal construction of this act, would hardly venture to amend the act, so as to read: "This act shall *not* have a reasonable construction—shall *not* be subject to the 'rule of reason' and shall *not* be interpreted by the 'light of reason.' "

It is urged that this leaves the law uncertain. True; but uncertainty is better than the ghastly certainty of business chaos, which would assuredly result if the law should be enforced according to its language as invalidating and penalizing every combination in actual restraint of trade. Verily, "the letter killeth" in this case.

Let us try to understand what literal interpretation and enforcement would mean in practice. It is difficult to arrive at a conclusion on this subject, since the most ultra-

radical of the supporters of a literal interpretation are staggered when presented by concrete instances. Take, for example, the most common case of a contract in restraint of trade, that is to say, of a contract in restraint of competition, namely, a partnership. Two individual dry goods merchants, competing with each other in interstate business, that is to say, in selling and shipping goods to the various States of the Union, combine and form a firm. Thereby competition is *pro tanto* eliminated. It is at once protested, of course, that that is not a violation of the Sherman Law. But why not? I have yet to hear any satisfactory answer to this question. It is certainly a contract and a combination. It is certainly in restraint of competition, and, therefore, in restraint of trade. If the statute is to be literally and impartially and thoroughly enforced, then every partnership between individuals engaged in interstate commerce must be enjoined.

So, when several individual competing manufacturers or traders carrying on interstate commerce unite to form a corporation, why is that not a combination in restraint of competition—that is to say, in restraint of trade? I have yet to hear any intelligible answer to this question. If the statute is to be equally and impartially enforced according to its letter, then every corporation whose stockholders formerly competed in interstate business must be enjoined, and this, of course, would cover a vast proportion of the manufacturing corporations in the United States.

A fortiori would this be true, where two or more corporations unite to form a third, to whom their properties are transferred, or where one corporation sells its business to another and agrees to go out of business itself.

A thousand similar instances can be suggested as to which the statute if literally construed would apply. What is said by the advocates of a literal interpretation to these instances? What tests do they lay down to discriminate between the cases where the law should be enforced and the cases where it should not be enforced? I have yet to hear any satisfactory answer to this question. Of course,

the test cannot be the magnitude of the interests involved—since that at once makes a basis of discrimination based upon considerations on which the judgment of courts may differ and *ipso facto* makes the law uncertain which they say ought to be certain and not subject to judicial discrimination.

The truth is, and there is no logical escape from the conclusion, that a literal interpretation and an impartial enforcement of the statute would stop the wheels of industry and would paralyze trade.

As President Roosevelt forcibly put the situation: "It is a public evil to have on the statute books a law incapable of full enforcement, because both judges and juries realize that its full enforcement would destroy the business of the country." (Annual Message to Congress, 2d Session, 59th Congress.)

I cannot believe that if the American people with their hard-headed common sense and sense of justice really understood what is meant by the clamor for a literal interpretation and enforcement of the law, they would tolerate it for a moment. Even on the lowest plane of self-interest, they would object to having the law applied to the thousands of combinations of small capital throughout the country. They may enjoy the slaughter of the Philistines; but they can hardly fall in love with suicide.

The law as interpreted by the Supreme Court has been sufficiently effective to catch some of the biggest fishes, the Beef Trust, the Standard Oil and the American Tobacco Company. The little fishes may well be allowed to escape through the meshes of the net.

After all, the whole basis of our Anglo-Saxon jurisprudence rests upon the discretion and discrimination of the courts, who work out for the community the rules of public policy guided by the light of reason. Better far the discretion of the courts than the discretion of the executive.

I have thus far considered the statute in its civil aspect, as affecting the right of the courts to apply remedies at law or in equity. When we come to consider the law in its

criminal aspect, we find ourselves confronted by a somewhat different and very serious situation.

Public opinion appears now to be clamoring for victims. It is not satisfied with damages or injunctions or possible receiverships, but punishment of individuals is loudly called for. Protests are even made against mere pecuniary fines. Actual imprisonment of the offenders is demanded. "Thumbs down" appears to be the state of mind of the spectators of the conflict between the government and the so-called "trust magnates". This state of mind is largely because of resentment at the results accomplished by the combinations and the power which they have acquired, rather than because of "righteous indignation" at the methods pursued in accomplishing the results or acquiring the power. The anger excited by the "swollen fortunes" of the multi-millionaires has much to do with this state of mind. We are in danger of losing our heads and of plunging into a crusade of vindictive attacks, not only upon capital, but upon capitalists. We are in danger of forgetting that even the rich man has rights which cannot be wantonly disregarded without danger to the poor man.

For myself, and at the risk of being out of accord with the present state of public sentiment, I do not hesitate to say, as I have said before in discussing this statute on public occasions, that the sweeping penal provisions of this law are unwise and unjust, and should be made more limited in their scope and much more definite and certain in their meaning.

Penal statutes involving personal punishment which are not based on moral distinctions are wrong in principle. To punish by imprisonment a man who has violated a prohibitory statute by performing an act which is *malum prohibitum,* but not *malum in se,* shocks the sense of justice. Of course, there are certain *mala prohibita* which are so clearly definable that personal punishment for a wanton disregard of them is appropriate; but such instances are exceptional. Where, however, the act which is *malam prohibitum* is not precisely defined, but is covered only by such

general language as "restraint of trade", personal punishment is unfair and unjust.

Restraint of trade is not *per se* an immoral act, nor is a contract or combination in restraint of trade *per se* an immoral transaction. Its morality or immorality depends upon the accompanying circumstances.

There may be and frequently are acts of moral turpitude committed in the creation or in the conduct of combinations in restraint of trade. Such acts of moral turpitude, if properly defined in advance, may well be made criminal.

Such acts of moral turpitude are, for instance, the use of unfair means to suppress competition and to crush out rivals, and agreement with competitors to raise prices or to restrict production.

To make "restraint of trade" criminal, irrespective of its character and purposes and irrespective of the methods pursued to accomplish the restraint, is to punish alike the intentional malefactor and the honorable and upright business man who has been guilty only of a technical violation of a prohibitory law. Especially is this true if the literal constructionists be taken at their word. If every contract or combination in restraint of trade is criminal, then as we have already seen the most ordinary and usual and hitherto innocent transactions may land a man in jail. Sales of business and good will, partnership agreements, formation of corporations between competitors in interstate commerce, all are illegal if the law be strictly enforced, and if the test of reasonableness or unreasonableness be not applied. There is absolutely no escape from this conclusion if the critics of the recent decisions of the Supreme Court were to have their way. The entire business community would be practically under the ban of the law and the jails of this country would not suffice to hold the criminals. No wonder that President Roosevelt said, with his customary vigor of language and force of expression:

"It is profoundly immoral to put or keep on the statute books a law, nominally in the interest of public morality, that really puts a premium upon public immorality, by

undertaking to forbid honest men from doing what must be done under modern business conditions, so that the law itself provides that its own infraction must be the condition precedent upon business success." [1]

The only escape from this condemnation of the penal features of this law is to apply the very test of reasonableness which the Supreme Court, as we have seen, has applied, not only in its latest decisions which have been so fiercely attacked by the literal constructionists, but in the Trans-Missouri and Joint Traffic Cases themselves.

So far as I can recall, the criminal features of the act have not yet come before the Supreme Court, except incidentally, as for instance, on the question of the right to examine corporate books before a Grand Jury and the application of the statute of limitations. What that court will hold when the criminal provisions of the Sherman Act shall come squarely before it, on an appeal from an actual conviction of an individual defendant indicted for "restraint of trade" is a debatable question.

It has been very forcibly urged that the statute, while sufficiently definite to support a civil suit, at law or in equity, is altogether too vague and indefinite to support a criminal indictment. The absence of all definition of what constitutes restraint of trade or monopolization would seem to leave to the arbitrary decision of a petit jury what acts should be criminally punished.

Here, again, however, we find the recent decisions of the Supreme Court to be clarifying in that they have supplied a distinction between what are legal and what are illegal restraints of trade and to that extent have made the statute more definite and certain. Not *all* contracts or combinations in restraint of trade, but only those in *undue* restraint of trade are criminal. True, it must be left to the jury to say what is a *due* and what is an *undue* restraint of trade. Nevertheless some test is laid down and the jury must exercise the same function as in many other

[1] President Roosevelt's Annual Message to the First Session of Sixtieth Congress.

cases where under proper instructions from the court, they are called on to pass in criminal as well as civil cases upon questions of due care or undue recklessness or negligence, or other similar questions.

The probabilities are that in view of its previous decisions on the questions heretofore submitted to it, the Supreme Court will uphold the penal provisions, if the indictment be sufficiently specific as to the overt acts and if the jury be properly instructed as to the necessity of finding that the "restraint" was "unreasonable" or "undue".

But whether the Supreme Court does or does not uphold the criminal provisions as sufficiently definite to be enforced, I submit that it is unwise and unjust and fraught with danger to individuals engaged in business enterprises to leave the penal provisions in such general language and covering acts not *per se* immoral. The criminal provisions should be amended so as to be made more specific and so as to bring within their scope only acts involving moral turpitude and clearly definable.

There are three evils to be apprehended from combinations in restraint of trade and from monopolization:

(1) Crushing out of competitors.
(2) Increase of prices to consumers.
(3) Decrease of prices to producers of raw material.

So far as any one of these evils is the result of unfair business methods, such unfair business methods are not only matters for civil cognizance, but may properly be remedied by penal statutes, which shall prescribe punishment to the offenders. Furthermore, any agreement or combination which has for its direct and immediate object the crushing out of competition or the increase of prices to consumers or the lowering of prices to producers may be regarded as *per se* immoral and may well be made not only illegal, but punishable criminally.

Various suggestions have been made looking toward other amendatory legislation. Certain ultra-radical champions of the anti-trust campaign are clamorous to overrule by new legislation the "rule of reason" decisions of the

Supreme Court in the Standard Oil and the Tobacco Cases. It is difficult to perceive how such legislation can be accomplished.

A proposition to enact that the statute shall *not* have a reasonable construction and shall *not* be interpreted by the "light of reason" is, as I have already pointed out, a proposition that can hardly commend itself to even the most radical of the critics of the Supreme Court.

A proposition to insert in the statute the words "reasonable or unreasonable" so that the statute should read "every contract or combination in restraint of trade, whether reasonable or unreasonable, shall be illegal," seems to be equally unthinkable. It is claimed that the Supreme Court has judicially legislated so as to insert the word "unreasonable" into the act. As a matter of fact, as I have already pointed out at some length, the court uses the word "undue" or "unduly," so that to meet the decision of the court, the statute would have to be amended so as to read "every contract or combination in restraint of trade, whether reasonable or unreasonable, whether in due restraint or in undue restraint of trade, shall be illegal." A statute reading in this language would be on its face, I submit, a contradiction in terms. A "due restraint" cannot be an "illegal restraint."

Another suggestion for amendment of the statute has the weight of the authority of the former President of the United States, who in his last annual message to Congress said: "I strongly advocate that instead of an unwise effort to prohibit *all* combinations, there shall be substituted a law which shall expressly permit combinations which are in the interest of the public, shall at the same time give to some agency of the National Government full power of control and supervision over them."

This was in accordance with his often expressed division of trusts into "good trusts" and "bad trusts." According to President Roosevelt's scheme, as advocated in his message, this power of "control and supervision" was to be exercised "not by judicial but by executive action, to

prevent or put a stop to every form of improper favoritism, or other wrongdoing."

This idea of Federal control by executive action has been carried further and made more explicit by others who have advocated a Federal license for corporations doing an interstate business, which license should be revocable in case of wrong-doing by any such corporation, or in case of a practical monopoly acquired by such corporation, by control of the whole or the greater part of any class of trade or commerce.

All these schemes for control by executive action, whether permissive or prohibitive, whether exercised by the President or by any subordinate authority, are, I submit, repugnant to our American traditions and principles. It has always been our boast that no one should be condemned except by the courts, after an opportunity to be heard and upon competent testimony. The Supreme Court said in Garfield v. Goldsby, 211 U. S. 262: "As has been affirmed by this court in former decisions, there is no place in our constitutional system for the exercise of arbitrary power." It seems to me incredible that the American people should consent to have their acts approved or condemned and their property rights and their business rights licensed or outlawed by executive mandate.

If this is to become a government by executive edict or by bureaucratic domination, the days of Republican institutions are certainly numbered. I for one am not prepared to admit that we are reduced to this extremity.

Another suggestion has been recently exploited and has the support of able advocates, namely, the creation by the Federal Government of a commission or a number of commissions who shall have power to regulate prices of articles of interstate commerce. This suggestion has been approved and advocated by some of the "trust magnates" themselves. It has even received the tentative approval of the Attorney-General in a recent public address as a scheme inviting consideration, though it has not received his definite approval or endorsement.

To my mind this is, with all due deference to its able advocates, an appalling suggestion. The imagination is staggered when one undertakes to think out soberly and calmly what the suggestion means. Articles of interstate commerce include all articles dealt in throughout the United States—the power to fix prices means the power of life and death to the various industries engaged in trade and commerce. Not only that, but it means the right to control the prices of the necessaries of life to the "ultimate consumer." What the average American and his wife and children shall eat and drink and wherewithal they shall be clothed depend upon the prices to be paid for such necessaries of life.

To confer such a power upon any body of men, however wise and however incorruptible, seems to me, as I have already said, appalling. Nothing short of omniscience can enable such a commission to perform its work with intelligence and with safety to the best interests of producer and consumer. The analogy of the Interstate Commerce Commission is an imperfect analogy. That commission has to do with a single subject—the regulation of railroads. The problems to be considered are comparatively simple; there are certain general principles common to all railroads which can be applied to the subject. Besides, the railroads are carrying on a public business and are charged with public duties.

The regulation of prices of a thousand articles of manufacture, affecting the business interests of millions of producers and the domestic affairs of millions of consumers, is a task from which the boldest man may well shrink.

Even if the law of supply and demand and the regulation of prices by competition have broken down and if the law against "restraint of trade" are not adequate to meet the situation—and if some remedy for the situation is necessary—we must surely find some remedy less revolutionary than this, which means arbitrary power in its most objectionable form.

I have refrained from discussing the economic questions

lying back of repressive and restrictive measures such as the Sherman Law. These questions are too far-reaching and too controversial to be appropriate to this occasion. I have assumed for the purposes of this discussion that the policy of the Sherman Law is a sound policy and that restriction and prohibition and penalizing of great combinations of capital are wise and expedient.

It is open to debate whether we have not made a step backward instead of a step forward in civilization towards the days of the anti-engrossing statutes of three centuries ago.

Certainly the law as it was supposed to stand before the recent decisions of the Supreme Court was decidedly a step backward. The prohibition of every contract in restraint of trade, whether reasonable or unreasonable, whether in due or in undue restraint of trade, was clearly a step backward and if enforced would have put an effectual embargo on business enterprises and would have paralyzed trade and commerce.

Is it not time to call a halt on further legislation against business interests and to let business adjust itself to the present law as interpreted by the Supreme Court? I am inclined to believe that the highest point of consolidation has been reached in manufacturing and trading enterprises and that hereafter under the operation of natural and economic laws the tendency will be to fall apart, to separate and to segregate. However this may be, I believe that the Sherman Law as interpreted and enforced by the Supreme Court is quite adequate, so far, at least, as civil remedies are concerned, to meet any further attempts at dangerous aggregations of capital. I protest against any further experiments in drastic legislation, especially in the direction of conferring arbitrary power upon the executive branch of the Federal Government which will be perilous, if not fatal, to our Republican institutions.

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