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CORPORATE OFFICER AND DIRECTOR AUTHORITY: THE PARAMETERS

I. INTRODUCTION

It is sad, but true, that Agency as an integrated body of jurisprudence has substantially disappeared from most law school curricula. Agency issues are recurrent in everyday practice and this body of law is fundamental to an understanding of how corporations act. In other words, without agents, we would wind up the “corporate doll” and it would do nothing. This article will examine the parameters of corporate officer and director authority.

II. DIRECTORS AUTHORITY: ITS REACH AND LIMITATIONS

It is fundamental in corporate law that the Board of Directors is empowered with the management of corporations. *See* MASS. GEN. LAWS ch. 156B §§47, 54. However, this concept does have its limitations. For example, directors do not bind a corporation through scattered individual member decisions, but rather by a collective exercise of judgment. *See generally Hurley v. Ornstein*, 311 Mass. 477, 42 N.E.2d 273 (1942). Additionally, while directors are invested with the management of the corporation and can delegate certain authority to agents (officers) of the corporation and in some cases to an executive committee (MASS. GEN. LAWS ch. 156B, §§ 47, 54), directors cannot create voting proxies, as a director has a fiduciary duty to exercise his own independent judgment. *See generally Saltmarsh v. Spaulding*, 147 Mass. 224, 17 N.E. 316 (1888); *Stoneman v. Fox*, 295 Mass. 419, 4 N.E.2d 63 (1936). The Board of Directors cannot sell substantially all of the assets of the corporation without the approval of the stockholders and directors cannot delegate all of their powers to an agent. *See generally Horowitz v. Slater*, 265 Mass. 143, 164 N.E. 72 (1928); MASS. GEN. LAWS ch. 156B § 75. The court voided a

contract entered into by the President of the BAA, whose principal function was the presentation of the Boston Marathons, designating the IMI as the exclusive promotor for 5-20 years. *See generally BAA v. International Marathoners, Inc.*, 392 Mass. 356, 467 N.E.2d 58 (1984). The court held that the BAA could not delegate total control or such broad authority that enables an agent to make extraordinary commitments or significantly encumber the principal asset of a corporation. *See generally id.*

III. SOME AGENCY ISSUES

An excellent starting point in exploring an officer's authority is with the case of *Mohr v. State Bank of Stanley*, 734 P.2d 1071 (Kan. 1987). This case reviews agency rules as they relate to corporate officer authority. If no actual authority exists for the act of the agent, the third party is generally left to argue apparent or inherent authority unless there is a corporate ratification. A third party is not allowed to rely on the representations of the agent as to his authority, but rather must inquire into the authority of the agent or rely on the appearances created by the corporation. *See generally Stoneman*, 295 Mass 419, 4 N.E.2d 63; *see also Rubel Hayden, Harding & Buchanan, Inc.*, 15 Mass. App. Ct. 252, 444 N.E.2d 1306 (1983). If express authority is inconsistent with those appearances, then it will not act in limitation of the apparent authority. *See generally Boston Food v. Wilson*. 245 Mass. 550, 139 N.E. 637 (1923). However, where evidence of apparent authority is either lacking or inconsistent, evidence denying the existence of actual authority may be adduced. *See generally Thalín v. Friden Calculating Machine Co.*, 338 Mass. 67, 153 N.E.2d 658 (1958).

The most difficult inquiry deals with the existence of inherent authority. Other than stating that this authority may be supported by what is customary within the business of the corporation, a black letter definition is difficult at best. It is this very difficulty that allows the courts a great deal of flexibility, creating situations where a court can back into a decision. For a decision where the apparent or inherent authority of a treasurer to execute a guarantee was examined, see generally *General Oversees Films Ltd. v. Robin*, 542 F. Supp. 684 (S.D.N.Y. 1982). *See also American Union Financial Corp. v. University National Bank*, 358 N.E. 2d 646 (Ill. 1976); *Keystone Leasing v. People's Protective Life Insurance Co.*, 514 F. Supp. 841 (E.D.N.Y. 1981) for cases examining the authority of a corporate clerk to certify the existence of a corporate resolution. The most common invocation of the inherent authority rule in the corporate context will occur when the president acts for the corporation.

The more traditional view is that the authority of the president is limited. More recently, however, courts have been willing to entertain liability, especially where the president acts in the capacity of a general manager. Keep in mind that all the other customary bases for authority exist including statutory authority. *See generally* MASS. GEN. LAWS ch. 156B, § 115. Although there are conflicting authorities in this area of the law, frequently a rational basis for the different decisional results is found in the facts. *See generally Lydia Pinkman v. Gove*, 298 Mass. 53, 9 N.E.2d 573 (1937).

IV. AUTHORITY OF THE PRESIDENT

In view of the broad statutory authority granted to directors and that the issue of authority of a lower rank officer is rarely presented, the most commonly raised questions concerning corporate authority deal with a president acting without an express grant of authority from the Board of Directors or the by-laws. Sometimes the president appears to have greater authority than what is accommodated by the facts or the law because of some special position as a result of substantial stock ownership or membership on the Board. However, it should also be remembered that when a president is acting in that capacity, that stock ownership or a position on the board do not generally expand his authority. *See generally Treasurer v. McDale*, 262 Mass. 588, 160 N.E. 434 (1928); *Wiley and Foss, Inc. v. Saxony Theaters, Inc.*, 335 Mass. 257, 139 N.E.2d 400 (1957) where the president of the defendant who was also a stockholder and member of the Board bound the corporate defendant, not because of his equity position or membership on the Board, but because the court found apparent authority. However, see generally *Jackson v. Colonial Provision Co., Inc.*, 314 Mass. 177, 49 N.E.2d 726 (1943) where the court held that the president's testimony as to his authority without objection warranted a finding as to authority to negotiate for the defendant corporation.

While the trappings of a particular office are not conclusive as to the officer's authority (see generally *Kanavos v. Hancock Bank and Trust*, 14 Mass. App. Ct. 326, 439 N.E. 311 [1982]), the extent of a president's authority will, to some degree, be determined by whether he is simply president or the general manager and/or chief executive officer as well. A president, at least if he is a general manager and more than simply an officer who presides at Board of Directors' meetings, will have the power to do what is usual and customary in the business, (see generally *Schwartz v. United Merchants and Manufacturer's Inc.* 72 F.2d 256 [2d Cir. 1934] and *Merchants National Bank v. Dunn Oil Mill Co.*, 73 S.E. 93 [N.C. 1911]). The general rule that a person dealing with an agent must inquire into the

extent of the authority, usually does not apply to a general agent who will be deemed to have inherent authority or apparent authority in an apparent authority situation. Of course, whether a specific action taken by a president is within his usual duties is a question of fact. See *Joseph Greenspons Sons Iron and Steele Co. v. Pacos Valley Gas Co.*, 156 A. 350 (Del. 1931).

V. THE AUTHORITY TO HIRE COUNSEL, COMMENCE OR DEFEND SUITS

The question of the president's authority to hire counsel or bring suit on behalf of the corporation frequently arises where there is a director deadlock. A corporation may be dissolved on account of director deadlock by filing a complaint pursuant to MASS. GEN. LAWS ch. 156B, § 99. A complaint to dissolve must be filed in the Supreme Judicial Court. See generally *Garrity v. Garrivv* 399 Mass. 367, 504 N.E.2d 617 (1987). However, as to the president's authority in a deadlock situation, there is very little case law in Massachusetts and no statutory law. Indeed very few jurisdictions empower the president of a deadlocked corporation.

Although the questions should come down to an objective examination of the president's authority, the courts will frequently decide the issue based on the equities because these cases are presented to the equity side of the court in terms of the remedy. As such, it should be no surprise that authority in the president to commence litigation is found more often when the president has a financial interest or the suit is brought against an officer or director.

One other item that needs to be considered is that courts generally are opposed to complaints for dissolution. A suit brought by a president under the right circumstances in a deadlock situation may be the lesser of the two evils for the court.

The general principal set out in *Lloydona v. Dorius*, 658 P.2d 1209 (Utah 1983), that the Board of Directors is vested with the management of the corporation is the principle that controls this issue and, therefore, generally the president has no authority to hire counsel. In *Lloydona*, the court set out an exception to the general rule, i.e., the president or other executive officer needs no resolution where the assets will be dissipated unless action is taken. *Id.*

There are three important cases in Massachusetts that deal with the issue of hiring counsel and a president's authority to bring suit in a deadlock situation. In *Kelly v. Citizens Finance Co.*, 306 Mass. 531, 28 N.E.2d 1005 (1940), an attorney brought suit against the corporate defendant to

recover his legal fees where the president (who was also a director) hired the attorney to defend a suit brought by a stockholder to dissolve the corporation. The court sets out the general proposition that "the authority to manage the business affairs of a corporation is primarily vested in its Board of Directors. Its president and treasurer, merely as the holders of those offices, have little or no inherent power to bind the corporation outside of a comparatively narrow circle of functions specifically pertaining to their offices." *Id.* at 532, 28 N.E.2d at 1006. The court goes on to say that in the cases where a president or treasurer has been held to have a general authority to make contracts, it will be found that such authority springs from either an express grant through a by-law or vote or grant of power as a general manager or impliedly by reason of continued exercise of similar powers in such a manner that knowledge and approval by the directors can be inferred. *Id.* at 532, 28 N.E.2d at 1006. In the *Kelly* case, the court held that the defense of such an actual lawsuit would not fall within the familiar duties of a president. *Id.* at 532, 28 N.E.2d at 1006.

On this issue of hiring counsel, since Mass. Gen. Laws. ch. 156B § 54 authorizes the Board of Directors to manage the corporation, this includes the authority to engage attorneys. However, a member of the Board of Directors who has an interest in a loan remaining unpaid is not allowed to vote. *American Discount Corp. v. Kaitz*, 348, Mass. 706 206 N.E.2d 156 (1965).

One of the cases cited by the *Kelly* Court in which a president brought a law suit on behalf of a corporation is the landmark case of *Lydia Pinkham v. Gove*. 298 Mass. at 53, 9 N.E.2d at 573. The authority was traced back to a broad grant in the by-laws; however, upon a closer examination, the result is arguably based more on the equities than on a true resolution of the authority issue. The president was a stockholder who was a member of the oppressed group of directors in that the defendant treasurer controlled the financial aspects of the corporation. The treasurer refused to liquidate loans to the corporation by the oppressor group of directors paying higher than market rates of interest and manipulated the financial statements to maintain a net worth below the number at which the by laws would require a dividend. While the court expressed some doubt concerning the unusual nature of the lawsuit, it nevertheless found authority in the supervisory functions of the president as based in the by-laws and expanded by vote. Of course, this was a deadlock situation where the president was a stockholder. However, even where no deadlock exists, some jurisdictions tend to recognize authority in the president or general manager of a close corporation where these officers are substantial shareholders. See generally *Westview Hills, Inc. v. Lizau Realty Corp.*, 160 N.E. 622 (N.Y. 1959); *Cicero Industrial Development Corp. v. Roberts*, 312

N.Y.S.2d 893 (1970); *Zimmerman v. Hog & Allen*, 209 S.E. 2d 795 (N.C. 1974); 2 O'Neal, *Close Corporation* Sec. 805 (3rd Ed.).

VI. CONCLUSION

Agency issues are frequently overlooked in corporate litigation, at least at the early stages. It is imperative to a sound analysis of the client's case that these matters are considered at the earliest possible time, as a contract with a corporation executed by an agent without authority is no contract at all.

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