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LIABILITIES OF ORGANIZERS, MEMBERS AND OFFICERS OF A PRIVATE CORPORATION UNDER THE INDIANA LAW

ROBERT W. MILLER*

By a concurrent resolution, approved March 1, 1927, the last General Assembly provided for the appointment of the Indiana Corporations Survey Commission to investigate the organization, operations, activities and control of private corporations in the state of Indiana, with the view of enacting a new Corporation Act.¹ The liabilities discussed in this article are the present liabilities imposed by our laws and affect all corporations now in existence. As will be seen, a Uniform Business Corporation Act is much in demand and the Corporations Survey Committee can do an excellent piece of work for Indiana by the proposal of a new Corporation Act.

I

PROMOTERS

A promoter is one who brings together the persons who become interested in the enterprise, aids in procuring subscriptions, and sets in motion the machinery which leads to the formation of the corporation itself. It is the promoter's work which brings the corporation into existence.

While ordinarily a promoter ceases to be such when the corporation is fully formed and the business turned over to the directors, such is not necessarily the case. As long as the work of formation continues, those carrying on such work retain the character of promoters.²

* See biographical note, p. 121.


² A promoter may also be an incorporator, subscriber, shareholder, director or other officer in a private corporation, and, in the usual case,
The promoters of a corporation are not the agents of the corporation before it comes into existence, for there cannot be an agency unless there is a principal. Since promoters are not the agents of a corporation not yet formed, it follows that a contract made by them does not bind the corporation, when formed, in the absence of a statute, adoption, or a provision in the charter to that effect. This question of personal liability of promoters by reason of contract will be discussed later.

The chief place where the tort liability of promoters is in question is where a fraudulent prospectus is issued. If the promoters of a corporation put forth a fraudulent prospectus, or otherwise make fraudulent representations, and such actions of the promoter cause third persons to become interested in the corporation's shares and securities to the damage of such third persons, a direct action exists in favor of such persons against those who have been guilty of the fraud, to recover such damages.

Individual liability also exists where the promoter commits any other tort such as trespass, conversion, nuisance, negligence, etc., and, under the rule that where several join actively in the promotion of a corporation a joint and several liability for the fraud and false representations of the others exists, one of several promoters may thus be liable for the torts of the others. The general rule that the tort feasor is liable for his torts applies does occupy one or more of these positions. However, for the sake of clarity the liabilities of each group of such persons individually will be considered and where a promoter does occupy more than one relation to the corporation, his liabilities will be considered as the sum total of the liabilities of each group under which he may be classified. In this article, preference has been given to Indiana and Federal decisions where such are in point, an effort being made to present the liability aspect from the point of view of Indiana decisions.

2 *Smith v. Parker* (1897), 148 Ind. 128. However, it is well settled that they occupy a fiduciary relationship to the corporation when it comes into existence and to the subscribers prior to its organization, while acting as promoters. *Cushion Heel Shoe Co. v. Hartt* (1914), 181 Ind. 167.

3 A contract made by the promoters of a corporation is not binding upon the corporation when formed unless such a contract was made upon the corporation's credit and with the mutual expectation that the promoters would form the corporation and that the corporation would assume the contract. *Davis Bldg. Co. v. Hillsboro Creamery Co.* (1893), 10 Ind. App. 42. The act of the corporation in adopting contracts entered into by promoters prior to its creation is considered, by the weight of authority, as a novation or the making of a contract by the corporation as of the date of such adoption. *Smith v. Parker* (1897), 148 Ind. 128.

as well to individuals who are acting in the capacity of promoters, as to any other individual.

The liability of promoters by reason of contracts has been fairly well settled by Supreme Court decisions. Promoters are personally liable on contracts entered into personally, even though made for the benefit of the projected corporation and though the corporation has been formed and has received the benefit of the contract. However, they are not personally liable where the contract is made in the name and solely on the credit of the projected corporation, provided such intention is clear to both parties of the contract and that neither express nor implied representations that there is an existing corporation have been made. This exception falls, however, if the contract entered into is one which the corporation when formed has no power to ratify or adopt. A promoter who makes a contract in behalf of a corporation to be organized, providing there is no provision exempting him from liability, is personally liable on such contract. In the absence of statute, however, promoters are not personally liable on a contract made in the name of the corporation after it has acquired a complete corporate existence.

A question of prime importance in the fixing of promoters' liability is the duty due from them to the proposed corporation and the corporation after it is formed. Needless to say, the promoters occupy toward the corporation and towards the persons who become shareholders therein a fiduciary relation. They must act with the utmost good faith in their dealings on behalf of and with the corporation and its stockholders, and will be liable to the corporation, either at law or in equity, according to the circumstances, for any fraud or breach of trust.

The general rule is that promoters must account for any secret profit made by them, this rule applying only where they are acting for the corporation, or a fiduciary relation otherwise exists, or where there is fraud. However, there is no rule of

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5 Bonsall v. Platt (1907), 153 Fed. 126.
7 O'Rorke v. Geary, 207 Pa. St. 240. Promoters are personally liable for obligations when they assume to contract in the name of and on the behalf of the corporation before it has acquired even a de facto organization. Heisen v. Churchill (1913), 205 Fed. 268.
10 Promoters will either be compelled in a proper action to refund any secret profits made by them while acting for the corporation, or in dealing with the corporation without a full and fair disclosure of the facts, or the
law which prevents a person who owns property, although pur- 
chased by him for the purpose, from promoting a corporation 
and selling the property to the corporation after its organization. 
It has been stated, however, that the promoter should follow one 
of four courses to make the contract with the corporation abso-
lutely binding where such a transaction is had.11 

The Supreme Court has held that no action will lie against the 
promoters for sale of property to the corporation at a large profit 
to themselves, when at the time of the transaction the promoters 
owned all the stock of the corporation, no profit being realized 
until later when a sale to the public was had. The Court was of 
the opinion that the profit had to be made at the time of the 
alleged illegal act in order for accounting to be required.12 

Before considering the liability of promoters to purchasers of 
stock, the liability of one promoter to another should first be 
ated. As a general rule, where the contract is definite and the 
obligations are clear, an action at law will lie at the instance of 
one promoter against a second for breach thereof upon failure to 
ceed with the promotion.13 Liability of promoters between 
themselves is usually based upon some agreement, though none 
is necessary. Promoters occupy a position of trust and con-
fidence, hence good faith is essential. On this basis one pro-
moter may compel others guilty of fraud or breach of trust by 
corporation may recover damages for the fraud at law or in equity, or in a 
proper case rescind the transaction and recover what is parted with. Paker v. Boyle (1912), 178 Ind. 560.

11 Four methods are: (1) Provide an independent board and make a 
full disclosure to the corporation through them; (2) make a full disclosure 
of all material facts to each original subscriber of shares in the corpora-
tion; (3) procure a ratification of the contract after disclosing its circum-
stances by vote of all the shareholders of the completely established corpor-
ation, or (4) person may himself be the real subscriber of all the shares of 
the capital stock contemplated as a part of the promotion scheme. Old 
Dominion Copper Co. v. Bigelow, 203 Mass. 159. The above four safe-
guards are used in order to protect the corporation from entering into a 
fratulent or harmful contract with the promoter. 

12 Old Dominion Copper Co. v. Lewisohn (1908), 210 U. S. 206. The 
Massachusetts case, supra note 11, is contra to the federal rule and holds 
that it is no defense that the promoters at the time of the transaction were 
the only stockholders. Davis v. Las Ovas Co. (1913), 227 U. S. 80, holds 
that promoters who join in defrauding the corporation by false repre-
sentations or concealment, or by fraudulently taking a secret profit, or pro-
moters and third persons who participate with them in the fraud, are joint-
ly and severally liable for the whole loss thereby sustained by the cor-
poration. 

taking a secret profit, misappropriating funds, etc., to account
in equity. Also, where one promoter pays a debt for which the
other promoters are liable, he is entitled to contribution.14

In addition to the liability to the corporation, a separate liabil-
ity exists to individual stockholders. In fixing this liability, an
examination of the prospectus is extremely important. Of
course, promoters may enter into any special agreement with the
subscribers or purchasers of the stock which is legal, and thereby
fix their liability. Where the ones originating the scheme, after
procuring the money to be paid in, abandon it, certain Illinois
cases hold that the subscribers may recover back the money paid
without any deduction for expenses incurred.15 A liability may
also arise where fraudulent representations induced the de-
frauded subscriber to subscribe, or where concealment of the
true facts was had. An action of deceit will lie against such
promoters.

The above liabilities constitute in general those imposed upon
a promoter of a private corporation.

II

INCORPORATORS

The state creates the corporation upon the application of
individuals who are called incorporators. This application is
usually made by signing and presenting the incorporation papers
to the proper officer.16 Broadly stated, corporators need only
have the capacity to contract, no other qualifications being re-
quired in the absence of statute to the contrary.

Hence, to form a corporation under a general law, the corpo-
rators or members must have the qualifications and must be of
the number prescribed by statute; and there must be at least

15 Lang v. Blocki, 286 Ill. 91. One who subscribes for stock in a corpora-
tion which fails to complete its organization may recover the money so paid
from the one to whom he paid it; but, in order to hold any or all of the
promoters of an abortive corporation, he must show that the person so re-
ceiving the money sought to be recovered was authorized to receive it for
the corporation, and that he, in fact, did so receive it. Fitzwilliam v.
Travis, 65 Ill. App. 183.
16 "Whenever three or more persons shall desire to form a corporation,
they shall prepare, sign and acknowledge, in duplicate, before a notary
public and file with the Secretary of the State, articles of incorpora-
tion. . . ." Burns' Statutes (1926), Sec. 4825.
substantial compliance with the provisions of the act, unless they are merely directory or conditions subsequent, in order to have a de jure corporation. A failure to comply with the statute in these respects would not, however, preclude the existence of a de facto corporation.

A number of our modern statutes require each subscriber to the articles of incorporation to subscribe for at least one share, writing after his name the number of shares he takes. Where such a statute exists the question arises as to the time when such signatories to the paper become actual shareholders as distinguished from persons who have agreed to become shareholders. In an early Indiana case it was held that the subscribers of the incorporation paper might elect the directors even before the recording of the instrument.\(^\text{17}\)

Where the enabling act does not require the corporators to become stockholders, the chief duty of the incorporators is to organize the corporation and set it in motion.\(^\text{18}\) Often, however, the incorporation laws require that the incorporation paper shall fix the number of the directors, and shall state the names of the first directors.\(^\text{19}\)

It is a very common practice for the incorporators not to be the substantial promoters of the enterprise, but only mere clerks or dummies. The courts have judicially disapproved of this practice, declaring such to be foreign to the intent of the incorporation laws.\(^\text{20}\)

Where an enterprise proves unsuccessful for want of sufficient funds to meet the statutory requirement, personal liability exists on the part of the corporators to return to the subscribers funds collected, regardless of whether the failure is due to conspiracy, fraud or negligence. Incorporators who permit a portion of their number to divert funds subscribed for the enterprise to an

\(^{17}\) *Covington Plank Road Co. v. Moors* (1852), 3 Ind. 510.

\(^{18}\) Danforth, J.: "The corporators are the associates who are the getters-up of the company, and whose functions cease with its organization. Corporators exist before shareholders, and do not exist with them. When stockholders come in, corporators cease to be." *Chase v. Lord*, 77 N. Y. 1.

\(^{19}\) It is not necessary to state in the incorporation papers the names of the first directors unless the statute requires it to be done. *Miller v. Gravel Co.* (1875), 52 Ind. 51. But where such a clause is had, it is deemed mandatory and a total failure to comply therewith renders the incorporation open to attack. *Reed v. Richmond St. R. R. Co.* (1875), 50 Ind. 342. In the light of this, some incorporation laws provide that corporators shall act as directors during the first year.

\(^{20}\) *Wechselberg v. Flour City National Bank* (1894), 64 Fed. 90.
unauthorized purpose, are guilty of negligence and breach of trust and liable to subscribers who suffer loss thereby.

For exemption from personal liability to be available to incorporators, all material requirements of the enabling act must be complied with. Where the assumption of the corporate privilege was naked, the associates have uniformly been held to full liability to the other contracting party, assumption being naked where business is transacted without recording the certificate of incorporation, filing or publishing same as required by law, etc.

There are but very few decisions dealing with the liabilities of incorporators as such. Incorporators are often promoters and stockholders as well; hence they have a merged liability.

III
SUBSCRIBERS

Subscribers to a corporation are those who on the formation of a corporation agree mutually to take and pay for the shares of capital stock, and, in the absence of any special provision, they agree with each other to pay therefor the par value of the stock. Strictly speaking, a subscriber is one who has agreed with the corporation to take a certain number of shares in the corporation by original issue, the term not being the same as stockholder.

As stated previously, some states require incorporators to set opposite their names the number of shares which they desire to take in the corporation. This is sufficient to constitute them sub-

21 Of course if the corporators carry on business before recording the certificate or performing other conditions precedent to incorporation, they may be subject to a partnership liability (unless there be a de facto corporation) as members of an unincorporated association. Ryland v. Hollinger (1902), 117 Fed. 216. Where an association of persons have complied with the provisions of the law necessary to constitute them a corporation, and have fixed the amount of their capital stock, but have not divided it, and in this situation contract debts, the individual members are jointly and severally liable for such debts. Hawes v. Anglo-Saxon Co., 101 Mass. 385. Where a contract is made in the corporate name after the articles of incorporation have been filed, but before any subscriptions have been obtained, and before an organization meeting has been held or officers elected, the incorporators are liable on the contract as partners. McVicker v. Cone, 21 Ore. 353.

22 Collateral attack is permitted to the other contracting party to hold incorporators to their partnership liability, but not other members of the company where there is only naked assumption.
scribers and, even where not required by statute, still there is nothing illegal in incorporators subscribing for stock in this fashion. Where such subscription is had, it is held that any such subscriber may retract or cancel his subscription before the paper is recorded with the consent of all his co-subscribers. As soon as the incorporation paper has been signed and duly recorded, each subscriber is irrevocably bound to accept the number of shares for which he signed. The rule is sometimes had that an agreement to take shares entered into by executing the incorporation paper of a projected corporation cannot, at least in England, be rescinded for fraud on the part of the promoters. The Indiana rules on this point are contra. Hence, in general, we may say that the obligation of subscribers of an incorporation paper is to pay the par value of the shares for which they subscribed, in installments when called in by the proper authority; this obligation only being fulfilled by taking shares from the company and not by transfer from another stockholder.

A contract of subscription for stock in a corporation, when binding, is a contract between the corporation and the subscriber; a valid contract being required to constitute a person a subscriber. No matter whether a subscription is made before or after the formation of the corporation, an offer by the one party and acceptance by the other is essential, the contract being one to take and pay for the stock upon the terms and conditions stated in the offer.

Where an agreement to form a corporation and to take stock therein is entered into, the intention of the parties being to contract with the corporation, such subscription is considered as a continuing offer to the proposed corporation, and becomes a binding contract as soon as the corporation is formed and ex-

23 Heaston v. Cincinnati R. R. Co. (1861), 16 Ind. 275. Where a person intends to become a corporator, he cannot without some further act or offer on his part be held as a subscriber to the capital if the company is incorporated by other persons. Richmond St. R. R. Co. v. Reed (1882), 83 Ind. 9.

24 Cravens v. Eagle Cotton Mills Co. (1889), 120 Ind. 6.

25 Wert v. The Crawfordsville Turnpike Co. (1862), 19 Ind. 242.

26 Butler University v. Scoonover (1887), 114 Ind. 381. A subscription for stock and a contract to purchase stock from a corporation are not the same, the latter not making the purchaser a subscriber or stockholder until it is executed by delivery of the certificate of stock. Such a tender is not a condition precedent in the case of pure subscription.
pressly or impliedly accepts the same.\(^{27}\) In the case of subscriptions after a corporation has been formed and is in existence, an offer and acceptance of such offer is essential in order to bind both subscriber and corporation.\(^{28}\) Hence, a subscription for stock cannot be revoked by the subscriber after it has been expressly or impliedly accepted by the corporation, a binding contract then being had which permits of withdrawal, if at all, only with the consent of the other party.

Where subscription to stock is made prior to incorporation and formation of the company and in contemplation thereof, it is considered a condition precedent that the corporation shall be legally organized as contemplated in order for liability to attach to the subscriber upon his contract.\(^{29}\) If the subscription contract is entered into after the formation of the corporation, a showing of a de facto corporation is sufficient for the corporation to maintain an action upon the contract.\(^{30}\) There is seemingly a conflict, however, where the subscriber contracts on the basis that the corporation is a legally formed corporation, while in fact it is nakedly assuming corporate existence. Some jurisdictions apply the doctrine of estoppel and enforce the contract, while others hold such a good defense for the subscriber.

\(^{27}\) The fact that the corporation is not in existence at the time the offer is first made by signing the agreement does not prevent the corporation from accepting when formed. Miller v. Wildcat Gravel Co. (1875), 52 Ind. 51.

\(^{28}\) Junction R. Co. v. Reeve (1860), 15 Ind. 236. Since there must be mutual assent to constitute a binding subscription contract, a corporation formed for other purposes or with other powers than those contemplated by the subscribers can not enforce the subscription against non-consenting parties. In the absence of provision to the contrary, consideration is required for a binding subscription. Mutualy of obligation is required and if, for any reason, the corporation is not bound, the subscriber is not bound. Marion Trust Co. v. Bennett (1907), 169 Ind. 346. In the absence of statute or contrary provision, subscription contract may be informal. Brownlee v. Ohio I. & I. R. Co. (1862), 18 Ind. 68. But where a definite formulae is had, subscription contract must comply to be binding. Coppage v. Hutton (1890), 124 Ind. 401. Subscriptions may be implied by conduct. Overmyer v. Cannon (1882), 82 Ind. 457. Being a contract, both parties must be competent to contract; an infant's contract being voidable where no statute is had forbidding him to subscribe. Indianapolis Chair Mfg. Co. v. Wilcox (1877), 59 Ind. 429.

\(^{29}\) There must be, in the absence of estoppel, not merely a corporation de facto, but a corporation de jure. Indianapolis Furnace & Mining Co. v. Herkimer (1877), 59 Ind. 429.

\(^{30}\) Heaston v. Cincinnati R. R. Co. (1861), 16 Ind. 275.
In the case where a contract has been made for the issue of stock at a discount or for overvalued property, in spite of modern statutes expressly requiring money or money's worth, a conflict as to the position of the parties exists. The Supreme Court has held that where the corporation consists only of such persons who assented to the illegal issue, the corporation has no remedy against the subscriber. Where the corporation is composed of innocent shareholders an action may be maintained, some courts not permitting cancellation and enforcing full payment for the shares; while other courts hold the subscriber not liable. In the case where the interests of the creditor are concerned, such creditor stands in the same position as the corporation and in those jurisdictions holding the issue void, the creditor is deprived of his remedy. Other jurisdictions permit the creditor, where necessary, to force the subscriber to fully pay for the stipulated shares, cancellation of the shares not protecting the creditor in the least and the amount not yet paid being an asset of the corporation to which the creditors may have recourse. In any of these cases, the wisdom of the statutes or decisions must be determined by the amount of protection afforded to the public, the creditors, and the innocent shareholder. Certainly those jurisdictions which bluntly hold void the issue of stock for overvalued property or for property that is not legal payment, do not, in many situations, seem to serve best the interests of any one of these three groups.

Another problem is presented in case the defendant is not a subscriber but a subscriber's transferee. Of course, if he is a transferee with notice, actual or constructive, of the true state of the transaction, he is in no better position than his transferee. But if he is an innocent purchaser of a certificate as for fully paid and non-assessable shares, the corporation should not be allowed to maintain any action against him. Hence the corporation cannot cancel shares of a bona fide transferee of a subscriber. Where creditors seek to hold innocent transferees of subscribers, it has almost universally been held that the creditor

31 Scully v. Automobile Finance Co., 109 A. 49. Such a contract is considered as having a two-fold aspect: (1) To take the stock at a discount and, (2) to take the stock. The first, being illegal, is disregarded and suit is brought on the second.

32 Kanaman v. Gahagan, 230 S. W. 141.


34 Bawn v. Imperial Theatres, 115 A. 918.

must suffer, as he might properly be given a recovery against the corporate officials.\textsuperscript{36}

In this article the defenses available to a subscriber such as fraud, mistake, false representation, etc., will not be discussed, the assumption being that a valid contract of subscription is made and that no release or discharge of the subscriber effected.\textsuperscript{37}

The validity and effect of the contract of subscription and the liability thereby imposed upon the subscriber are to be determined in accordance with the laws of the state in which the corporation was created. In addition, the provisions of the corporate charter or of the general laws by which the corporation is governed becomes a part of the contract of subscription. Hence, the contract and the liabilities, there inflicted must be construed in connection with such laws and provisions.\textsuperscript{38} In all jurisdictions a corporation may maintain an action of assumpsit to recover the amount of a due and unpaid subscription, or of an assessment or call thereon, if there is an express promise to pay the same. Seemingly, most states imply a promise on the part of the subscriber to pay all valid assessments where a valid contract of subscription is had.\textsuperscript{39} In the case where the corporation

\textsuperscript{36} Supra, note 35.

\textsuperscript{37} A subscriber may be released in whole or in part from his contract by the corporation with the consent of all the other stockholders; but he cannot withdraw and surrender his shares without the consent of the corporation; nor can he do so with the consent of the corporation, unless all the other stockholders consent; nor can he do so with the consent both of the corporation and all the other subscribers, if the amount due from him is required to pay corporate debts.

A subscriber is released by forfeiture of his stock to the corporation for non-payment of assessments, but not by a sale of his shares to pay assessments, where, under the charter, he is liable for any deficiency.

A subscriber is released by a valid transfer of his shares, whereby the transferee takes his place, and assumes his liability as a shareholder. Clark on Contracts, p. 403.

\textsuperscript{38} Falmouth and L. Turnpike Co. v. Shawhan (1886), 107 Ind. 47.

\textsuperscript{39} Millier v. Wild Cat Gravel Road Co. (1875), 52 Ind. 51. A call is an official corporate declaration requiring a prescribed part of subscriber's stock to be paid for at once. Calls to be valid must be made in the manner prescribed, by the person or board designated, and must operate uniformly on all the stockholders. Liggett v. Glenn (1892), 51 Fed. 381. Where the time is fixed for payment a call is not necessary, but otherwise where the time of payment is to be fixed by the directors or stockholders. Banty v. Buckles (1879), 68 Ind. 49. Assessment signifies statutory payments levied by the corporation upon the holder of its shares, over and beyond the par value of its stock. Interest runs on assessments from the time they are
seeks to recover for the amount of calls, it may either wait until
all become due and collect or sue as each call becomes due. How-
ever, all installments which are due must be recovered in a single

In summary, the liability of a subscriber may be said to be
based upon the subscription contract. The contract is the meas-
ure and extent of his liability which, generally speaking, may be
said to pay the par value of the shares subscribed for and, in
addition, to meet all calls and assessments which are properly
levied. The liability of a subscriber is not absolutely clear due
to the fact that the subscriber usually becomes a stockholder and
thus there is a combined liability, with but few decisions separat-
ing this liability into its component parts.40

IV

STOCKHOLDERS

A subscription to any legal and valid instrument, by which a
person engages to become a member of the corporation when
organized, and to pay a given sum which is to be a part of the
capital stock followed up by an acceptance of a certificate for
the stock, will make such subscriber a shareholder of the corpo-
ration.41

A contractual relationship exists between the corporation and
shareholders, such contract to be interpreted in the light of the
corporate charter and by-laws, governing statutes, and the set-
tled law of the land.42 This relationship, even where the stock-
holder is personally interested, does not preclude him from

40 The proposed Uniform Business Corporation Act states the subscrib-
er's liability as follows: "A subscriber to or holder of shares of a corpora-
tion . . . shall be under no liability to the corporation with respect to
such shares other than the obligation of complying with the terms of the
subscription therefor; but one who became a shareholder in good faith and
without knowledge or notice that the shares he acquired had not been fully
paid for, shall not be liable to the corporation with respect to such shares."

41 A mere subscription to stock does not ipso facto constitute the sub-
scriber a stockholder. Wheeler v. Thayer (1889), 121 Ind. 64. Any con-
duct expressly or impliedly showing that the corporation recognized the
subscriber as a stockholder and that the subscriber assented to being a
stockholder is sufficient to constitute the subscriber a stockholder. Gowdy
Gas Well Co. v. Patterson (1902), 29 Ind. App. 261.

voting for a contract or other measure at a meeting of the corporation. Being permitted to deal with the corporation, profits made by him in the course of his dealings belong to him personally, the corporation or other stockholders having no interest therein. A shareholder may become a creditor of the corporation, and, where such does happen he stands on equal footing with the other creditors.\textsuperscript{43}

The capital stock and assets of a corporation belong to it and may be disposed of by it, if it does not violate its charter, as fully and freely as if it were a natural person, subject to statutory limitations and the right of creditors to attack any transactions as fraudulent. No direct trust, at least where the corporation is a going concern, attaches to its property in favor of creditors. As a general rule, however, statutes usually limit this right of a corporation to contract to "money or the true value in property."\textsuperscript{44}

The discussion on calls and assessments given earlier in this article is also applicable in a discussion of stockholders liability. Ordinarily, an assessment may be levied and collected on fully paid stock, where authority to do so is conferred by the articles of incorporation, or statute, or by agreement; but not otherwise.\textsuperscript{45} Generally, an assessment can only be levied upon persons who are stockholders at the time and a person who has ceased to be a shareholder, due to a valid transfer of his shares, etc., cannot be assessed.

Where a shareholder converts corporate funds, obtains property from the corporation by false representation, or is unlawfully holding corporate property, the corporation may maintain an action against him. The Courts will not permit a fraud to

\textsuperscript{43}The general and well settled rule is that contracts and dealings between a corporation and its stockholders are valid if the stockholders do not also act as the agents of the corporation in the matter and if no fraud is committed against other shareholders or creditors. There is nothing in the relation between a corporation and its stockholders which \textit{per se} prevents dealings between them.

\textsuperscript{44}A contract to take stock has two aspects: (1) to take the stock, and (2) to take such at a discount, where such is the essence of the contract. Hence, where the corporation issues its stock at a discount or for overvalued property and intends to so contract, the purchaser may still be liable for the balance—due to the first aspect of the contract; the second aspect being disregarded as contrary to statute. Although the corporation itself may be precluded from calling upon the stockholder for additional amounts, the creditor, in case of insolvency or where such payment is necessary to meet corporate debts, may sue and have payment made into the corporation.

\textsuperscript{45}\textit{Toner v. Faulkerson} (1890), 125 Ind. 224.
be committed on the corporation, especially where the rights of creditors and innocent stockholders are involved.

Hence, in general, it may be said that the chief liability of a shareholder to the corporation is upon his contract, but that, in addition, he is liable for any fraud, conversion, or other tort perpetrated on or in connection with the corporation or its property. Fair play is essential and in determining whether or not such transactions are honest, the enabling act, corporate charter and by-laws, and the law of the land must be closely scrutinized.

Where there has been a failure to incorporate or where there has been an attempt to form a corporation under an unconstitutional statute or for a purpose not authorized by statute, the persons attempting such an incorporation are held liable as partners where not even a de facto corporation is accomplished. A reason given for the personal liability of the associates is that there is no responsible body or corporation behind them; that, having no principal, they bind themselves individually. Sometimes the same result is reached on the basis of estoppel.46

The corporation is not the only party to whom stockholders may have to answer, for many times one stockholder may sue another. For instance, where one stockholder has paid more than his share of a corporate debt, he may enforce contribution from other shareholders. Contribution may be had where payment was made on account of statutory or subscription liability, but not where made on account of a penal liability.47 Minority stockholders may sue the majority where there has been a misappropriation of the corporate assets. Those who have paid assessments on their stock may sue to compel delinquent shareholders to pay or to have their liability declared. There are numerous cases in which one stockholder may sue another, but the above constitute the more common suits.

Heretofore, the liability of a stockholder to the corporation and to other shareholders has been considered. In addition to such liability, there are the rights of creditors to be considered. The capital stock of a corporation is the basis of its credit since, in the absence of statute, no personal liability is inflicted upon the stockholder for corporate debts. Hence, it would seem to

46 Persons who assume to act in a corporate capacity without a legal existence as a corporation, either de jure or de facto, are personally and individually liable as partners to those with whom they contract. Owen v. Shepard (1894), 59 Fed. 746.

47 Liability to contribute survives the death of a stockholder. Allen v. Fairbanks (1889), 40 Fed. 188.
follow that where persons deal with a corporation on the faith of this fund, that such persons may insist that it shall be paid in, when its payment is necessary for the satisfaction of their claims against the corporation. Such has been held to be the law, shareholders of an insolvent corporation being compelled to pay the amount due on their stock into the corporation to satisfy corporate debts. The liability to so pay in is based, by some courts, upon the trust fund doctrine that the capital stock is a trust fund for the benefit of creditors. However, it is very difficult to see that this is the true basis for such a liability and many courts have overthrown the trust fund doctrine as the basis for such a rule.

The above liability rests in contract, being an indebtedness to the corporation itself and not to the creditors. Each subscriber is liable for the full amount due on his stock, irrespective of whether all of the stockholders can pay or whether such other stockholders are insolvent. The creditor, in order to maintain his action, must be a judgment creditor who has not waived his right or released the stockholder.

At common law, stockholders were not liable at all to the creditors of the corporation unless the corporation was insolvent and they were indebted to the corporation on account of their stock, payment being necessary to pay corporate debts to creditors; or unless the capital stock of the corporation, or a part of

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48 Marion Trust Co. v. Blish (1908), 170 Ind. 686.
49 Unpaid subscriptions are like any other assets of the corporation when it becomes insolvent, and may be collected, like any other asset, through the interposition of a court of equity for the purpose of paying its debts, and if the corporation has secretly agreed not to require payment, or if it has released the subscribers without consideration, the agreement or release may be held void as against creditors on the ground of fraud. Hospes v. N. W. Mfg. & Car Co., 48 Minn. 174.
50 See v. Heppenheimer, 69 N. J. Eq. 36.
51 In addition it must be shown that the corporation is insolvent, that the stockholder sued is liable to pay for such stock, that such stock has not been paid for in full, and the existence of a debt or debts for which the amount of the collection is to be paid on. The fact that stockholders are subject to an additional liability imposed by statutes does not protect them from payment of the full purchase price of their shares.

The question of permitting of set-offs often arises. Where the corporation is known to be insolvent, shareholders who are also creditors cannot set off their debts against their liability for the par value of their stock. Where, however, the corporation is a going concern, the tendency has been to permit such a set-off. In the former case, however, the stockholder must pay for the stock and then come in with the rest of the creditors for his claim.
it, had been unlawfully distributed or paid out to them. However, the Legislature clearly has the power to impose individual liability for corporate debts upon shareholders, if such is done at the time of creation of the corporation. Hence, we come to the statutory liability of stockholders.52

In a number of states, provisions have been placed in the constitution, or statutes have been passed, tending to make shareholders individually liable for the debts of the corporation. Such provisions and statutes vary from state to state and, in some states, from time to time. In some, perhaps the liability is unlimited, while in others liability only in proportion to either the amount or value of the stock held is had. In still other states double liability is had, while in still other states the liability is limited to the amount due on the stock. Hence, it can readily be seen that the extent of the liability can only be ascertained by a study of the governing statute.53

The statutory liability imposed may be either contractual or penal.54 The effect of the statute and not the form determines its character. Where penal, the right of contribution by one stockholder against another is cut off.

The question is inevitably raised as to whether the liability of the shareholders is joint or several. Under those statutes holding shareholders liable for corporate debts to the amount of their stock for which they have subscribed, but not paid, seemingly it would be best to construe the liability as several. Where no limit is had for corporate debts, their liability seems to be joint. Indiana holds that in the absence of anything showing a contrary intention on the part of the legislature, that the liability imposed is several where such liability extends to the amount of or to a proportion of the stock held by such stockholder.55

52 Stockholders are not personally liable for the debts of the corporation in the absence of a statute to that effect. Gainey v. Gibson (1897), 149 Ind. 58. The stockholders of a corporation are not individually liable for its torts if they have not in any way participated therein, in the absence of a contrary statute or provision. Hartzles v. Goshen Churn and L. Co. (1914), 55 Ind. App. 455. Of course, shareholders may render themselves personally liable for corporate debts by agreement to that end, provided sufficient consideration is had. Thompson Estate Co. v. Weinhard (1918), 247 Fed. 951.

53 Ordinarily, the liability of a stockholder for corporate debts is to be determined by the laws governing the formation of the corporation and not the laws of the state of the shareholder's residence.

54 A statute which directs or prohibits some act and imposes some forfeiture for its violation is a penal statute. Otherwise, the courts construe such as contractual. Flash v. Conn. (1883), 109 U. S. 371.

55 Shafer v. Moriarty (1874), 46 Ind. 9.
LIABILITIES OF ORGANIZERS

For whose benefit is this statutory liability imposed? The liability is not imposed for the benefit of the corporation and is not to be construed in any sense as a part of its assets. The corporation has no right to exercise this benefit for the creditors, even where suit against the stockholder is had for the purpose of raising a fund for the payment of debts. The provisions of each statute must be consulted in order to tell for whose benefit liability is imposed.

A perusal of the statute must also be made before answering the question as to whether the statutory liability is primary or secondary. In some jurisdictions there is an express statutory provision that creditors must first look to the tangible assets of the corporation before enforcement of statutory liability is permitted. Where a single shareholder is proceeded against and recovery had from him, a right of contribution against the other stockholders is allowed him, even though a several liability is imposed by statute.

Hence, in general statutory liability depends entirely upon the express wording of the statute and a close study should be made of it in determining the stockholders liability in the various states.

Statutory liability having been imposed upon the stockholders, the next question naturally arising is as to who are liable under such statutes. It would seem to follow that every person in whose name, as owner, stock is registered on the books of the corporation, with his knowledge and consent, would be liable. The conflict arises where a transfer of shares is had, some states holding the transferor liable, others the transferee, and still others both. The statute imposing the liability should cover this point so as to remove all doubt upon the question. Where a transfer is made to a man of straw or an insolvent person, all jurisdictions hold that the transferor does not thereby escape

66 Hammond v. Cline (1908), 170 Ind. 452.
67 Where liability is primary, creditors may sue and collect from the stockholders to the extent of their liability without first resorting to the assets of the corporation and exhausting their remedies against it. Where the liability is secondary, all remedies against the corporation must first be exhausted, judgment and unsatisfied execution being a condition precedent to their right to hold the stockholders upon their statutory liability.
69 Some courts have held that creditors may waive statutory liability for corporate debts. Morfield v. Cincinnati, etc. Traction Co. (1924), 144 N. E. 689. It is doubtful whether other jurisdictions will follow the result reached in this decision.
liability, where such was the purpose of the transfer. In the case of a bona fide purchaser from a subscriber of shares expressed to be fully paid, without notice that, in fact, such were not fully paid for, the best authority seemingly excuses such purchaser from paying the unpaid balance into the corporation where the creditors seek to enforce such payment. It would seem better to excuse the innocent purchaser from such liability and permit the creditor an action against the transferor, although the argument can be made that the innocent purchaser might have his action against the transferor.

Another question of prime importance is the liabilities of Stockholders in an Indiana Banking Corporation. Sec. 6 of Art. 12 of the State Constitution provided: “the shareholders of every bank or banking company shall be individually responsible to an amount over and above their stock, equal to their respective shares of stock, for all debts or liabilities of said bank or banking company.”

Sec. 3858, Burns’ Statutes, 1926, provides: “the shareholders of each bank or association found under the provisions of this act shall be individually liable to an assessment of not to exceed one hundred per cent of the par value of their respective shares of capital stock, and in addition to all assessments for unpaid subscriptions for capital stock or parts thereof, same to be levied and collected as hereinafter provided, when such assessment is required for the payment of the debts or liabilities of such bank or association or to restore the capital stock thereof.” The balance of the section states the procedure for assessment and collection. Hence, in the light of these provisions, the stockholders liability to meet an impairment shall not exceed one hundred per cent, the top limit thereby enacted being a double liability.

Ohio Statute provides: “the holder of a certificate for shares purporting to be fully paid and non-assessable, who is without actual knowledge of the non-payment of the full amount of the consideration therefor, shall be under no liability whatsoever in respect thereof.”

Liability provided by Art. 12 of the Indiana Constitution is for the benefit of creditors of the bank. Furthermore, a shareholder who is also a creditor of the bank cannot set-off its indebtedness to him against his constitutional liabilities for its debts. Gentry v. Alexander, President of the Bank of Gosport (1861), 16 Ind. 471. In Runner, Assignee, v. Dwiggins (1897), 147 Ind. 238, the court held that the individual responsibility for all debts to the extent of the amount of their stock, in addition to the amount invested, was created exclusively for the benefit of creditors. Further, that it is not a corporate asset, the corporation having no right or interest in such statutory liability.
Returning again to the liability of stockholders in private corporations, other than banks, Sec. 4845 of Burns' Statutes 1926, provides: "Every stockholder shall be liable to the corporation for the par value of all stock owned by him, unless such stock has been paid for the corporation at its par value, or unless the articles of incorporation provide that such stock may be sold at more or less than its par value, in which case, the owner of stock shall be liable to the corporation only for the amount of the sale price fixed in such articles until such amount has been paid to the corporation."

Most of the states have statutes very similar to the above Indiana statute—the effect being to impose a liability upon the shareholder to the amount of his unpaid stock, for all corporate acts, until the whole amount of the capital stock subscribed for shall have been paid in. Seemingly, such a statute is to be commended, a double liability only being reserved in the case of banks due to the nature of their business and confidence reposed in them.

(To be continued.)