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Corporate Knowledge Required for Ratification by Acquiescence

Henry T. Jones

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assets of a competitor *rather* than the stock.²⁶ Both types of merger are now expressly made illegal providing the requisite effect on competition exists.²⁷ Aware of the previous strict construction the Supreme Court of the United States has given, mergers to be consummated by seeking the assets first as aforementioned are specifically forbidden.²⁸ A result of making acquisition of assets illegal is to bring down the other notable exception that of purchasing the stock, conceded to be unlawful, and acquiring the assets by surrender of the stock before the FTC held a hearing.²⁹

The comment to Congress by the FTC can be, better late than never, because for years corporations with the able assistance of the U.S. Supreme Court were rendering Section 7 of a nullity doing indirectly what they could not do directly.

HERBERT SAUL ROVNER.

CORPORATE KNOWLEDGE REQUIRED FOR RATIFICATION BY ACQUIESCENCE

A principal is liable for the act of his agent when the agent has authority to do the act or when after the act is done the principal ratifies it. When the authority is not given in the first instance the principal is required, after knowledge of the action taken, to affirmatively adopt or ratify the action as his own or he must fail to act affirmatively when the circumstances require such action if he is to be held liable for the unauthorized act. The latter is ratification by acquiescence. No act or ratification by the agent is sufficient. The ratification must be by the principal as he is the only one who had authority to authorize the act originally. It is the situation in which ratification by acquiescence is being proved that the knowledge of the principal becomes most important. These principles of ratification would seem to apply equally to a corporation.

The problems of the requirement of knowledge become more acute in the corporate situation where all action is by agents. There authority is delegated by the board of directors, and so it would seem that before there could be ratification by acquiescence of an unauthorized act the board of directors would have to be apprised of the act.

There may be ratification by acquiescence in case affirmative action is taken pursuant to the unauthorized contract, or there may be ratifica-

26. See note 2 for citation of amendment, *supra*.

27. See note 2 for citation of amendment, *supra*.

28. See note 2 for citation of amendment, *supra*.

29. Compare Section 7 (see note 1 for citation), amendment (see note 2 for citation) and cases in notes 15 and 16, *supra*, with each other.

tion by silence for an unreasonable time, or the corporation may be estopped to deny ratification.¹

In the first class, ratification by action pursuant to the contract, the conventional elements of ratification seem to be pretty much disregarded. It appears that corporate action pursuant to the contract, even with no showing of knowledge of the contract on the part of the directors, is enough to satisfy the courts that the contract should be enforced. In one case it was said that a continued practice of having checks cashed upon improper endorsement at least put the directors on notice, and the action was apparently ratified by the corporate officers.² Similarly, in *Farmers' State Bank of Riverton v. Haun*³ where there was a course of conduct on the part of the manager of endorsing notes in the name of the corporation which was not within his authority, it was held that the endorsement was ratified and that it made no difference that knowledge of the endorsements was obtained by the other directors at an illegal meeting. In cases such as these where there has been a course of conduct⁴ it would seem that there need be no mention of ratification but that the question could be determined on the basis of antecedent ostensible authority. If the decisions were based on such ostensible authority there would be no question as to knowledge on the part of the corporation which is a requirement of ratification.⁵ Indeed, these grounds have been used alternately to uphold a contract without any mention of the required corporate knowledge when referring to ratification by action on the agreement.⁶

There is less room for criticism of the decisions in which there was a continued course of conduct than of those which involve only one such unauthorized act, contract, or agreement. It would seem that in this type of case the required knowledge is also presumed or entirely overlooked, but here there is no course of conduct so as to create anything resembling ostensible authority. One example of skipping over the requirement of knowledge by the corporation was in a case in which it was held that

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1. This article is not concerned with express ratification by the corporation.
 2. *Newmark Grain Co. v. Merchants' Nat. Bank of Los Angeles*, 166 Cal. 203, 135 Pac. 958 (1913).
 3. 30 Wyo. 322, 222 Pac. 45 (1924).
 4. *Cox v. Baltimore & O.S.W.R. Co.*, 180 Ind. 495, 103 N.E. 337, 50 L.R.A. (N.S.) 453 (1913); *Heath v. Potlatch Lumber Co.*, 18 Idaho 42, 108 Pac. 343, 27 L.R.A. (N.S.) 707 (1910); *Southern Bitulithic Co. v. Hughston*, 177 Ala. 559, 58 So. 450 (1912); *Kimball Bros. Co. v. Citizens Gas & Electric Co.*, 141 Iowa 632, 118 N.W. 891 (1908); *Toni v. Kingan & Co.*, 214 Ind., 611, 15 N.E. (2d) 80 (1938); *Whitfield v. Kern* 122 N.J. Eq. 332, 192 A. 48 (1937); *Tennessee Products Corporation v. Broadway Nat. Bank*, 25 Tenn. App. 405, 158 S.W. (2d) 361 (1941); *Cache Valley Banking Co. v. Logan Lodge No. 1453 B.P.O.E.*, 88 Utah 577, 56 P. (2d) 1046 (1936).
 5. The case of *Arp & Hammond Hardware Co. v. Hammond Packing Co.*, 33 Wyo. 77, 236 Pac. 1033 (1925) came very close to such a holding where the president's running the financial affairs for 20 years with acquiescence of the other directors was held to be "equivalent to antecedent authority."
 6. *Newmark Grain Co. v. Merchants' Nat. Bank of Los Angeles*, 166 Cal. 203, 135 Pac. 958 (1913); *Crane Co. v. James McHugh Sons*, 108 F.(2d) 55 (W.D. Okla. 1939); *Hosack v. Taylor Bros.*, 142 Pa. Super. 83, 15 A.(2d) 489 (1940); *Tennessee Products Corporation v. Broadway Nat. Bank*, 25 Tenn. App. 405, 158 S.W.(2d) 361 (1941).

being ready to perform an unauthorized contract was sufficient to show ratification while in the dicta it was said it was sufficient even if the directors assented separately and not in the recognized manner of a duly convened meeting.⁷ Another example of disregard for knowledge or action by the board of directors was in a case in which the manager, without authority, entered into a contract to sell bottles. The contract provided that it should be invalid unless accepted by the home office. The company delivered part of the bottles and this was held to be not only sufficient to constitute acceptance of the contract but also an independent ratification of the manager's act.⁸ This would indicate that the court was not even thinking of ratification by action of the board of directors but that the act of delivery was sufficient to show ratification even though there was no mention of knowledge by the directors of the delivery. Again, a manager without authority issued an attachment bond to begin a law suit. After an adverse judgment the case was referred to the legal department which helped perfect an appeal. This was held to be a ratification by the corporation of the act of issuing the bond. There is no indication that the directors had knowledge of the act.⁹ In the two last mentioned cases there may have been good cause for holding the corporation to the agreement from which it was trying to extricate itself but there should have been other more clear grounds than ratification.

In the foregoing situations there have been some acts which the courts could point to as action by the corporation. When there is a failure to act on the part of the corporation other grounds must be found to hold the corporation to its agreement. Probably the most acceptable ground upon which such a holding is made is that of estoppel to deny ratification, or *estoppel in pais*. This applies when the corporation by its failure to act has led the other party to act and has accepted the benefits thereof. To come within the rule that the corporation is estopped to deny ratification it must be shown that the corporation had full knowledge of the material facts and accepted the benefits of the agreement.¹⁰ Still in this situation the knowledge requirement is not very strictly adhered to. It seems that so long as there is a clear case of benefit to the corporation the knowledge requirement is treated summarily. Such was the case in *First Nat. Bank of American Falls v. American Falls Canal & Power Co.*¹¹ in which the engineer in charge of the job authorized the bank to pay checks made out by him for labor. It was there held that the corporation was estopped to deny ratification without any mention of knowledge

7. *U.S. Fire Apparatus Co. v. G. W. Baker Mach. Co.* 10 Del. Ch. 421, 95 A. 294 (1915). See also, *Ochs v. Equitable Life Assur. Soc. of U.S.*, 111 F.(2d) 848 (E.D. Mo. 1940) where after action on the contract for two years knowledge was imputed. Cf. *Plowman v. Indian Refining Co.*, 20 F. Supp. 1 (E.D. Ill. 1937) where pension checks were paid but it was held that there was no ratification because there was no knowledge that the men were not working and there was nothing about the contract to pay same in the minutes of the directors' meeting.
8. *Cumberland Glass Mfg. Co. v. Wheaton*, 208 Mass. 425, 94 N.E. 803 (1911).
9. *State ex rel. Spellman v. Park-Davis & Co.*, 191 Mo. App. 219, 177 S.W. 1070 (1915).
10. *Fletcher Cyclopedia Corporations*, 1931, Vol. 2, Sec. 773.
11. 20 Idaho 368, 118 Pac. 668 (1911).

on the part of anyone authorized to issue such checks. There was, however, work performed which benefited the corporation for which the checks were issued. In another instance it was held that mere presence of the directors upon receipt of a check pursuant to an unauthorized contract was sufficient to constitute the knowledge required for estoppel to deny the contract.¹² In *Allen v. Central Counties Land Co.*¹³ it was held that the introduction of the payroll at the directors' meeting was sufficient knowledge to estop denial of an unauthorized employment contract. More attention is given to knowledge of the corporation when there is inter-dealing with the directors. Such was the situation in *Star Mills v. Bailey*¹⁴ in which the president borrowed money for the corporation from one of the officers. There was no authorization by the board of directors and it was held that there was not sufficient knowledge to establish ratification. Likewise, when the unauthorized contract has the effect of selling the corporation out of business, proper knowledge of the directors is more closely scrutinized.¹⁵

Ratification by acquiescence, when there is nothing but silence on the part of the corporation, is very close to estoppel to deny ratification but is a step removed in that there is no element of benefit to the corporation. When an agreement may not be sustained on the estoppel theory, plain ratification by acquiescence may be considered.¹⁶ The same rule applies in the case of ratification by acquiescence as in estoppel to deny ratification; that there must be full knowledge coupled with failure to disaffirm to constitute the ratification.¹⁷ In this, as in estoppel, more attention is paid to the knowledge factor when the transaction is with an officer or director of the corporation. So, in *Elk Valley Coal Co. v. Thompson*,¹⁸ where an unauthorized note was given to one of the directors in return for his part in effecting a sale of the assets, it was held that ratification of the sale at a meeting of the board was not a sufficient basis of knowledge for ratification of the note even though part of the directors had individual knowledge of it. The requirement is less stringent in other cases such as where a license to use a spur track was given, and it was said that by the use thereof the directors must necessarily have known of license and acquiesced in it.¹⁹ In another case the contract was made at an improper

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12. *Valley Lumber Co. v. McGilvery*, 16 Idaho 338, 101 Pac. 94 (1908).
 13. 21 Cal. App. 163, 131 Pac. 78 (1913). See Also, *Coldiron v. Good Coal Co.*, 276 Ky. 833, 125 S.W.(2d) 757 (1939), no mention of knowledge; *Magruder v. Hagen Ratcliffe & Co.*, 131 W.Va. 679, 50 S.E.(2d) 488 (1945), no mention of knowledge; *Webb v. Duvall*, 177 Md. 592, 11 A.(2d) 446 (1940), constructive knowledge.
 14. 140 Ky. 194, 130 S.W. 1077, 140 Am. St. Rep. 370 (1910).
 15. *Elk Valley Coal Co. v. Thompson*, 150 Ky. 614, 150 S.W. 817 (1912); *Beck v. Edwards & Lewis*, 141 N.J. Eq. 326, 57 A.(2d) 459 (1948).
 16. *Elk Valley Coal Co. v. Thompson*, 150 Ky. 614, 150 S.W. 817 (1912); *Belzoni Oil Co. v. Yazoo & M.V.R. Co.*, 94 Miss. 58, 47 So. 468 (1908); *Common Sense Min. & Mill. Co. v. Taylor*, 247 Mo. 1, 152 S.W. 5 (1912).
 17. *Fletcher Encyclopedia Corporations*, 1931, Vol. 2, Sec. 769.
 18. 150 Ky. 614, 150 S.W. 817 (1912).
 19. *Belzoni Oil Co. v. Yazoo & M.V.R. Co.*, 94 Miss. 58, 47 So. 468 (1908). See also, *Hamilton v. Shredded Wheat Sales*, 54 R.I. 285, 172 A. 614 (1934); *Briers v. Alderson*, 101 W.Va. 662, 133 S.E. 373 (1926); *Manheim Dairy Co. v. Little Falls Nat. Bank*, 54 N.Y.S.(2d) 345 (1945).

meeting and while it was decided on the theory of estoppel the court said that it could have gone on ratification by acquiescence in that the board, knowing of the action of the president of signing the contract, did not disaffirm within a reasonable time.²⁰

A basic rule of corporations is that the corporation can only act through a duly constituted meeting of the board of directors. It is also the basic rule of ratification that the principal must have full knowledge of the material facts before there can be any ratification.²¹ Whether or not acquiescence will amount to ratification depends upon the facts of the particular case.²² So it seems, also, with respect to the requirement of knowledge before there can be ratification by acquiescence. It would appear that the only way knowledge could come to the corporation would be in a duly convened meeting of the board of directors.²³ This, however, is not the knowledge which is actually required. In fact, it would appear in cases in which there had been action on the contract or a previous course of conduct that knowledge by the corporation was presumed rather than actual. This comes within the rule that the corporation will be deemed to have knowledge if the circumstances are such as to put a reasonable person on inquiry and such would reveal the facts.²⁴ Such circumstances are likely to be present when the corporation has acted on the contract or there is a previous course of conduct. The courts generally, however, skip lightly over the knowledge phase and make it appear that the action is the important thing. The foregoing is also true with respect to estoppel to deny ratification. In cases where the contract has been acted upon and, as in estoppel, where a benefit has been retained, there is more basis for saying that the circumstances would put a reasonable man on inquiry than in the situation in which there is only passive acquiescence. Still there is no strict requirement of knowledge of the board acting as a body, even in cases where the ratification is based on nothing more than passive acquiescence, with the possible exception of situations in which the transaction involves an officer or director of the corporation, or where the contract has the effect of selling out the business.

HENRY T. JONES

20. *Common Sense Min. & Mill. Co. v. Taylor*, 247 Mo. 1, 152 S.W. 5 (1912).

21. *Fletcher Cyclopedia Corporations*, 1931, Vol. 2, Sec. 756.

22. *Ibid.*, Sec. 770.

23. The knowledge could be obtained otherwise if it related to a matter, the authority over which was delegated to some agent of the corporation.

24. *Fletcher Cyclopedia Corporations*, 1931, Vol. 2, Sec. 757.