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Corporations, Partnerships, and Associations

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CONTRACTS

Because of the lack of significant opinions rendered on Contracts during the period covered by this survey, Professor Joe H. Munster, Jr. has not submitted an article this year.

THE EDITORS

CORPORATIONS, PARTNERSHIPS, AND ASSOCIATIONS

The significant decisions in this section of the 1962 survey of Ohio law are highlighted by: (1) a relaxation of the formalities required for director action, (2) a strict interpretation of the rule that dissolution does not terminate a corporation's obligations, (3) a consideration of what is a "successor" corporation, and (4) an imposing number of unfair competition cases.

APPROVAL OF CORPORATE CONTRACTS

Ohio Revised Code section 1701.54 is a practical answer to the informal internal proceedings of most closely-held corporations. It permits directors as well as shareholders to take any action without a meeting which could be taken at a meeting.¹ At the same time, the legislature has indicated its intention to make action without a meeting more difficult by requiring that approval of such action be both written and unanimous.²

In *Piening v. Titus, Inc.*³ the unanimous approval requirement was relaxed considerably and the writing requirement waived. The corporation involved had three shareholders, and two of them were also directors of the corporation. The non-director shareholder dissented from a change in corporate purpose and demanded the fair cash value of her shares. An offer to purchase the dissenter's shares was made by letter, signed by the company vice-president, a director-shareholder. The letter constituted his consent in both capacities to the offer. The evidence was conflicting as to whether the third shareholder, the company president, a director-shareholder, had also consented. If he did consent it was merely an oral authorization to his attorney who drafted the letter.

The court of appeals held that the president was accustomed to allowing his attorney to make decisions for him, and that there was sufficient

1. For a discussion of the reasons for the general rule that directors must act formally as a board, see 2 FLETCHER, CYCLOPEDIA OF CORPORATIONS § 394.1 (perm. ed. rev. vol. 1954).

2. See comments to OHIO REV. CODE § 1701.54 (Supp. 1962).

3. 113 Ohio App. 532, 179 N.E.2d 374 (1960).

evidence that the offer had his explicit or implicit consent. The decision says nothing about the consent of the third director, the president's daughter. The court ruled, however, that there was sufficient evidence that the unanimous consent requirement of the statute had been met. But, the court disregarded the statute's second requirement, that the consent be in *writing* and signed by all directors and shareholders. Waiver of the writing requirement was apparently based on the court's decision that the corporation should not be able to utilize its own faulty informal procedures to deny that it had entered into a valid contract. This result seems justified by the apparent authority of the vice-president to make the offer to purchase.⁴ Thus, the *Piening* case should not be relied on as precedent that courts will make a practice of relaxing the requirements of section 1701.54 in the future.

Another corporation found itself bound by the apparent authority of a corporate officer in *Goodride Tire Co. v. Albert-Harris, Inc.*⁵ The president of Albert-Harris had a far-reaching employment contract which gave him almost complete control of the company's activities.⁶ The corporation's regulations also gave him authority to sign contracts. Under these circumstances, the court of appeals held that Albert-Harris could not contest the president's apparent authority to sign notes binding the company.⁷

DISSOLUTION — ITS EFFECT ON CORPORATE BUSINESS

The general rule is that dissolution terminates the actual business life for which a corporation has been created, but it does not terminate all corporate business.⁸ “[L]ike an individual after death, its activities must be settled; its claims collected, its debts paid, its sums due the state satisfied.”⁹ The strict adherence to this rule by Ohio courts is exemplified by the recent decision of the Ohio Supreme Court in *Commonwealth Tel. Co. v. Bowers*.¹⁰

The Ohio public utility excise tax is a privilege tax levied on July 1

4. A corporation, like an individual, may find itself bound by the apparent authority of its agent. 12 OHIO JUR. 2d *Corporations* § 404 (1955).

5. 114 Ohio App. 276, 181 N.E.2d 719 (1960).

6. The scope of authority of a corporation's agents is determined in the first instance from their contracts of employment. 12 OHIO JUR. 2d *Corporations* § 404 (1955).

7. Another significant recent case which held that officers and directors of a closely-held corporation frequently act informally, but nevertheless have authority to bind the corporation is *In re B-F Building Corp.*, 284 F.2d 679 (6th Cir. 1960). This case was discussed in the 1961 survey of Ohio law. See Gafford, *Survey of Ohio Law — Corporations, Partnerships, and Associations*, 13 W. RES. L. REV. 457 (1962).

8. 13 OHIO JUR. 2d, *Corporations* § 936 (1955).

9. *American Oak Leather Co. v. Peck*, 63, 108 N.E.2d 179, 183 (Ohio B.T.A. 1951).

10. 174 Ohio St. 141, 187 N.E.2d 30 (1962).

for the succeeding fiscal year.¹¹ In the case of a telephone company, the tax is levied on the privilege of furnishing telephone service. Commonwealth entered into an agreement to sell all of its assets to a new corporation controlled by General Telephone and Electronics. A certificate of dissolution was filed by Commonwealth on June 30, 1960, but approval of its plan of reorganization was not obtained from the Public Utilities Commission until July 1, 1960. Commonwealth then conveyed its assets to the new corporation on July 2, 1962.

The supreme court held that Commonwealth had operated for one day in the 1960-1961 fiscal year, July 1, and must pay the entire 1960-1961 excise tax of \$36,174.60.¹² The court pointed out that Commonwealth existed to furnish telephone service to the public until the commission approved its plan of reorganization. Filing a certificate of dissolution did not terminate its telephone business, so it was required to pay the excise tax.¹³

The *Commonwealth* decision points up the traditional procedure of filing the certificate of dissolution first and then winding up the corporation's affairs. It is often better to reverse this procedure and wind up the corporation's affairs before dissolving.¹⁴ Dissolution cannot be relied upon to terminate corporate obligations, or as shown by this decision, even corporate business.

DISREGARD OF CORPORATE ENTITIES

Is an existing corporation the same corporation as the one which preceded it? This question was presented to a common pleas court in *Richmond Heights Gen. Hosp. v. Blue Cross*.¹⁵

Ohio Revised Code section 1739.06 permits Blue Cross to offer a different rate of reimbursement to non-profit hospitals which have been in existence for a year or more than to those which have been in existence for less than a year. Blue Cross had found it necessary to institute two rate formulas because of the problems presented to hospitals in their first year of operation. Richmond Heights General Hospital, a new corporation, asked the court to declare it to be the successor to Forest Hills Hospital. This would permit Richmond Heights to qualify for the more beneficial Blue Cross rate given to hospitals which have operated for a

11. OHIO REV. CODE §§ 5727.31, 5727.32(I).

12. Additional Ohio authorities on the effect of dissolution on a corporation's obligation to pay taxes include *American Oak Leather Co. v. Peck*, 108 N.E.2d 179 (Ohio B.T.A. 1951) and *State v. Brown*, 121 Ohio St. 73, 166 N.E. 903 (1929).

13. For a general discussion on the effect of dissolution on the payment of taxes see 16A FLETCHER, CYCLOPEDIA OF CORPORATIONS § 8129 (perm. ed. rev. vol. 1961).

14. The timing of dissolution is irrelevant from a federal income tax standpoint. Rev. Rul. 54-518, 1954-2 CUM. BULL. 142.

15. 184 N.E.2d 626 (Ohio C.P. 1962).

year or more. Richmond Heights had taken over all of the personal property and staff of Forest Hills and moved them to a new building. This was the only physical change, but it was accompanied by a change in legal entities.

The court held that the essential fact in determining whether Richmond Heights was the successor to Forest Hills was not whether it was the same legal entity as its predecessor but whether it was "continuing in the experience of its predecessor."¹⁶ The court concluded that Richmond Heights was the successor to Forest Hills, and that the change of corporate articles was one of corporate form rather than substance.¹⁷ Richmond Heights's staff had the experience of more than a year's operation, and the court held that Richmond Heights should not be denied the benefits of that experience simply because of a change in corporate form. The court also seems to have indicated that corporate forms should be disregarded to a greater degree when hospitals are involved than with other corporations. "A hospital more so than other corporations is not merely a group of stockholders."¹⁸

In another case involving a hospital, *Shaker Medical Center Hosp. v. Blue Cross*,¹⁹ a court of appeals again looked to the substance rather than the form of a hospital's operations in determining the issue before it. The court held that the mere fact that a hospital is *incorporated* not for profit is not sufficient to qualify it as a "non-profit hospital."²⁰ The hospital also must be *operated* on a nonprofit basis. In this case the evidence proved that the hospital was operated primarily for the benefit and profit of the doctor who was the sole owner; therefore, it did not qualify for Blue Cross assistance to "nonprofit hospitals."

UNFAIR COMPETITION

The problems involved in protecting trade names and trade secrets and in avoiding situations from which liability might arise through the wrongful use of the trade names and trade secrets of another, are well illustrated by a variety of Ohio cases reported during the past year.

Trade Names

In *National City Bank v. National City Window Cleaning Co.*²¹ a court of appeals held that a bank was entitled to an injunction to prevent

16. *Id.* at 628.

17. For discussions of what constitutes a "successor" corporation see *Whitaker-Glessner Co. v. Strick*, 25 Ohio App. 415, 158 N.E. 554 (1927); 15 FLETCHER, CYCLOPEDIA OF CORPORATIONS § 7203 (perm. ed. rev. vol. 1961).

18. *Richmond Heights Gen. Hosp. v. Blue Cross*, 184 N.E.2d 626, 628 (Ohio C.P. 1962).

19. 115 Ohio App. 497, 183 N.E.2d 628 (1962).

20. OHIO REV. CODE § 1739.01(B) (Supp. 1962).

21. 180 N.E.2d 20 (Ohio Ct. App. 1962), *rev'd & remanded on other grounds*, 174 Ohio St. 510 (1963).

a window cleaning company from using the words "National City" in its name. The court found that the bank deserved this protection even against a non-competitive business to prevent the public from being confused into thinking that the window cleaning company had the bank's sponsorship. This decision goes further in granting trade name protection from non-competitive businesses than any other previous Ohio decision.²² It also goes further than the decisions of many other jurisdictions.²³

Trade Secrets

The law is clear that even in the absence of an express contract, a former employee or business associate may be enjoined from utilizing trade secrets or "confidential information" revealed to him in confidence during his employment.²⁴ The problem generally presented to the courts is: what is a trade secret, and what is "confidential information."²⁵

In *Commonwealth Sanitation Co. v. Commonwealth Pest Control Co.*²⁶ the use of the trade name "Commonwealth" was enjoined but the use of customer lists by two former employees was not. The former employer argued that his customer lists were "confidential" because restaurants and hotels which use pest control companies do not want the general public to know that they have need for such services. The court held that customer lists sometimes can be protected as "confidential"; however, what the customers think of the lists is not the determining factor. What is important is the availability of the customers' names to the general public. In this case anyone who had been associated with the pest control business would know what types of customers to contact. One

22. In *Henry Furnace Co. v. Kappelman*, 91 Ohio App. 451, 108 N.E.2d 839 (1952), the plaintiff's trade name was protected from a non-competitive business, but plaintiff and defendant were both in the furnace business though one was a manufacturer and one a retailer. In *Hugo Stein Clock Co. v. S. B. Stein & Son*, 58 Ohio App. 377, 16 N.E.2d 609 (1937), protection from a non-competitive business was also given to plaintiff's trade name. However, despite the fact that plaintiff and defendant sold non-competitive products, they were both retailers located on the same street within close proximity of each other.

23. In the recent case of *Wills v. Alpine Valley Ski Area, Inc.*, 118 N.W.2d 954 (Mich. 1963), the Michigan Supreme Court refused to grant an injunction to stop a ski area from using the name "Alpine," which had been used for six years by the plaintiff, a sports shop. The sports shop, among other things, sold ski clothing and ski equipment. The court ruled that the businesses were non-competitive and that the evidence presented did not indicate that the use of the same name by both businesses would so confuse the public as to substantially injure the sports shop.

24. Annot., 165 A.L.R. 1453 (1946); *Hance v. Peacock*, 169 N.E.2d 564 (Ohio C.P. 1960). A former employee may use his "experience, skill, acumen, memory and general knowledge" to engage in a competitive business, but he may not reveal trade secrets related to him in confidence by a former employer. *Perfect Measure Tape Co. v. Northeis*, 93 Ohio App. 507, 513, 114 N.E.2d 149, 152 (1953).

25. For a definition of "trade secrets" see 52 OHIO JUR. 2d *Trade Secrets* § 1 (1962).

26. 178 N.E.2d 518 (Ohio Ct. App. 1961).

could do so by looking up restaurant and hotel numbers in a telephone book. The court concluded that lists compiled in this manner are not "confidential" and their use would not be enjoined.

In *Stranges v. Fliehman*²⁷ a former partner entered into the same business as the dissolved partnership from which he had been bought out and began soliciting its customers. The other partner sought an injunction to prevent the solicitation on the basis that it was impairing the business's good will. Unlike the *Commonwealth* case, there was no contention that customer lists were confidential nor that a similar business name was being used. The court held that in the absence of an agreement not to compete, the former partner had an absolute right to engage in the same business, provided he did not represent himself to be the successor to the business and entitled to its good will.

A change of employment may result not only in a charge of the unauthorized use of trade secrets by a former employee and his new employer, but the new employer may be charged with the unauthorized pirating of employees for the purpose of obtaining trade secrets. These charges were made by the B. F. Goodrich Company after a key man in its space suit program was hired by International Latex. However, a common pleas court ruled that

the mere fact that a former employee or one who possesses a trade secret has accepted employment with a rival manufacturer isn't sufficient to warrant an injunction against the employee unless the circumstances are such as to persuade one that the ulterior purpose of such hiring is evil.²⁸

The court went on to hold that B. F. Goodrich had failed to prove that its former employee had been pirated away to obtain trade secrets and had failed to prove that the employee had actually revealed any trade secrets.²⁹ On this basis, the injunction was denied.

This brief survey indicates that Ohio courts have gone further than many jurisdictions in granting trade name protection. At the same time, the difficulties of proving that information in the hands of a former associate or employee qualifies for trade secret or "confidential information" protection should be evident.

27. 182 N.E.2d 19 (Ohio C.P. 1961).

28. The case has not been officially reported but is discussed in the Wall Street Journal, Feb. 25, 1963, p. 8, col. 5.

29. Another recent suit concerning the pirating of employees was filed by the First California Co. against Eastman Dillon, Union Securities & Co. First California sought two million dollars from Eastman Dillon for conspiring with several First California employees to hire away other First California employees for the purpose of expanding Eastman Dillon's California accounts. The case was recently settled. *Corporation Law and Tax Report 2* (Dec. 31, 1962). However, it points up the fact that while individual employees may be recruited from competitors, where there are no long-term employment contracts involved, it is unlawful to recruit as a part of a general conspiracy to take over a part of the competitor's operations.