Marquette Law Review

Volume 5
Issue 1 *Volume 5, Issue 1 (1920)*

Article 6

1920

Differences Between Corporations By Estoppel and De Facto Corporations (in Wisconsin)

David Charness

DIFFERENCES BETWEEN CORPORATIONS BY ESTOPPEL AND DE FACTO CORPORATIONS

(IN WISCONSIN.)

There is, in the law of private corporations, a great confusion existing, between estoppel to deny corporate existence and de facto corporations. Some courts do not make any distinction nor seek to make any discrimination, but prefer to use the terms interchangeably, one overlapping the other. Even our own state court has in certain decisions, referred to the one term when the other should have been used. Thus they say in one case: "Every fact points to an honest belief on their part that they had formed a valid corporation and we, therefore, conclude that the corporation was at least a de facto corporation. Being such, and the defendant having dealt with it on that basis, he is estopped from saying that there was no legal corporation at least so far as transactions within its supposed corporate powers are concerned."[1] In an earlier case, the court says: "We hold that the defendant cannot raise the question of the existence of the corporation on the grounds of estoppel. As to the defendant, the plaintiff as a corporation de facto, is sufficient."[2] Some courts hold expressly, that the doctrine of estoppel to deny corporate existence applies only to associations that are at least de facto corporations; that it does not apply to associations possessing no color of corporate existence.[3] To limit the rule of corporations by estoppel to de facto corporations, gives rise to a mere anomaly. By the weight of authority, everyone but the state is estopped to deny the corporate existence of a de facto corporation. There would certainly then, be no valid reason to invoke the doctrine of estoppel, where there really exists a de facto corporation. As clearly stated by one writer: "Where there is a de facto corporation, it is unnecessary to invoke the doctrine of estoppel, as the general rule of public policy forbids anyone but the state raising the question of corporate existence."

From an analysis of the decisions of this state, it seems that a de facto corporation need not exist to estop third parties from

---

[1] *Gilman vs. Druse*, 111 Wis. 400.

[2] *Black River Improvement Co. vs. Holway*, 85 Wis. 344.

[3] *Jones vs. Aspen Hardware Co.*, 21 Col. 263, 268, 52 American S. R. 220.

denying the corporate existence of a pretended corporation. Probably the best discussion of this principle is found in the two cases involving the defendant, Head. In *Slocum vs. Head*[4] and *Clausen vs. Head*,[5] the court held the defendant not a de facto corporation. In the first case, the plaintiff had treated the defendant as a partnership, and the court so adjudged it to be. In the latter case, the plaintiff had treated the defendant as a corproation and had so dealt with it. The court, therefore, held the defendant to be a corporation by estoppel as against the plaintiff. As stated in the second case: "If the appellant in the transaction out of which the alleged claim arose, dealt with the association as a corporation, such dealing, by estoppel as to such transaction, fixed the status of the company to be what it was represented and recognized to be therein." It is thus to be noted, that our court held a third party could be estopped from denying the corporate existence of an association, although such association was not a de facto corporation.

In another case our court says that whether the certificate is sufficient to prove the incorporation or not, or whether any defects in it are cured, it seems to be unnecessary to determine. The execution of a mortgage to a corporation is an admission of its corporate existence and estops the mortgagor from denying the same.[6]

Perhaps the most clinching argument for our statement, is found in *Citizens' Bank vs. Jones*,[7] where the court says: "Without determining whether the plaintiff payee was at the time of the execution of the note a de facto corporation within the meaning of the authorities, yet, we are constrained to hold that both Mr. and Mrs. Jones, (defendants), by the execution and delivery of the mortgage, are estopped from denying the corporate existence of the plaintiff."

Justice Marshall, in a rather recent opinion remarks:[8] "We note what counsel says as to persons holding policies in the name of the so-called new company not having participated in and so perhaps, not being bound by, the adjudication that such company is not a corporation in any sense and may hold it to be otherwise

[4] *Slocum vs. Head*, 105 Wis. 431.
[5] *Clausen vs. Head*, 110 Wis. 405.
[6] *Witney vs. Robinson*, 53 Wis. 309.
[7] *Citizens' Bank vs. Jones*, 117 Wis. 455.
[8] *Huber vs. Martin*, 127 Wis. 412.

on the doctrine of estoppel. We are not unmindful of the rule in that regard and that in some circumstances it extends beyond corporations de facto and includes such cases as that of a collection of persons falsely assuming to be a corporation, where there is no semblance of corporate existence. It does not apply, however, where the parties knew or ought to have known, the reasonable belief in the corporate existence and reasonable reliance thereon, does not exist." This case simply brings out the rule in Wisconsin that the doctrine of estoppel of third persons to deny corporate existence is not predicated upon the doctrine of de facto corporations but exists of itself, where the parties have so dealt with one another to infer that there existed a transaction with a legally incorporated body.

As to wherein a corporation by estoppel resembles a de facto corporation, is our remaining inquiry. A de facto corporation can exist only when there is a valid law under which a de jure corporation could have been created and an unconstitutional law is not sufficient to support a de facto corporation.[9] Some courts have held that on the theory that the doctrine of estoppel is limited to de facto corporations, there is no estoppel to deny the existence of a pretended corporation, where there is no law under which it might exist, or what amounts to the same thing, if the statute under which it claims to exist is unconstitutional.[10] However, the contrary and the weight of authority, holds that the existence of the doctrine of estoppel to deny corporate existence does not depend at all upon the right to be a corporation, or on the existence of a corporation de facto, and therefore, persons who hold themselves out as a corporation or who deal with a pretended corporation, may be estopped to deny incorporation, whether there is any valid law authorizing such a corporation or not or whether the law under which the pretended corporation is operating, has expired.[11]

A corporation expressly prohibited by statute or contrary to public policy, cannot escape liability under the defense of de facto existence.[12] Likewise, according to the weight of authority, the doctrine in relation to estoppel to deny corporate existence does

[9] *Martin vs. Huber,* 127 Wis. 412, and *Gilkey vs. How,* 105 Wis. 41.

[10] *Brandestein vs. Hoke,* 101 Cal. 131, and *Jones vs. Aspen Hardware Co., supra.*

[11] *Black River Improvement Company vs. Holway,* 85 Wis. 344.

[12] *Evenson vs. Ellington,* 67 Wis. 634.

not apply where a pretended corporation is expressly prohibited by statute or where it is contrary to public policy.[13]

Without going into the authorities, it can be said that members of a de facto corporation are as immune from personal liability as are members of a de jure corporation. By the weight of authority, the rule that a person contracting with a corporation as such is estopped to deny its corporate existence, applies so as to prevent him from denying its corporate existence for the purpose of maintaining an action on the contract or on an implied contract against the stockholders or members individually, unless they have been guilty of fraud or there are other circumstances rendering the doctrine of estoppel inapplicable in the particular case.[14] In the Wisconsin case, the court says: "Where a person deals with what he supposes is a corporation, with what all parties think is a corporation, where he gives his credit to that supposed corporation, he cannot afterwards, when it turns out that it is not validly incorporated, turn around and say, 'Well, I dealt with this supposed corporation; I thought it was a corporation but it seems when it first attempted to become incorporated, that there was some defect or irregularity in its proceedings, so that it did not become legally incorporated and therefore you who are stockholders will be held personally liable'." The Federal rule is in accord with this Wisconsin decision.[15] It is to be particularly noted that in the case just referred to, the court refused to hold the association a de facto corporation, but nevertheless held it a corporation by estoppel and the members free from any personal liability to the plaintiff.

A de facto corporation can sue in contract or in tort, with the same effect as can a corporation de jure, while an association of individuals, who are a corporation by estoppel, as to certain persons, can sue such persons only as a corporation in an action upon contract.[16] It is said in this case: "Where a person enter into a contract with a body purporting to be a corporation, and such body is described by the contract by the corporate name which it has assumed, or is otherwise clearly recognized as an existing

---

[13] *Hossack vs. Ottowan Development Association,* 244 Ill. 274 and *Fletcher on Corporations*—Vol. 1, 336.

[14] *Clausen vs. Head,* 110 Wis. 405, 85 N. W. 1028 and 14 *Corpus Juris,* 231.

[15] *In re Western Bank,* 163 Federal 713 and 68 N. W. 370.

[16] *Citizens' Bank vs. Jones,* 117 Wis. 446.

corporation, such person thereby admits the legal existence of the corporation for the purpose of any action that may be brought to enforce the contract, and will not be permitted by a plea of nul tiel corporation, to deny the legality of its corporate existence." Other Wisconsin cases are in accord.[17] As to actions in tort, by such corporation by estoppel, it may be said that where a corporation by estoppel, which is not a de facto corporation, brings an action to recover for or to enjoin a trespass or other wrong, there is no principle on which the defendant can be held to be estopped to deny the corporate existence of the plaintiff and its capacity to sue unless he has in some way, in connection with the alleged wrong, dealt with or recognized it as a corporation.

This permission to sue upon all transactions arising out of the theory of estoppel to deny corporate existence, extends to all cases where a third party deals with an association as a corporation, in the particular proceedings on hand. Thus, the Wisconsin courts have held that he who gives a note to a corporation is not to be permitted to deny that there is such a corporation, in a suit brought by the corporation by estoppel, if such it can be termed, against the maker of the note.[18] Our court has also held that the execution of a mortgage to a corporation is an admission of its corporate existence and estops the mortgagor from denying the same.[19] This rule applies to deeds granted to associations, as corporations.[20]

Mere dealing with an association under a corporate name, according to the weight of authority, does not estop one from denying corporate existence.[21] The doctrine does not apply, in the words of Justice Marshall, to a case where the parties know or ought to have known the true situation, for the essential element, the reasonable belief in the corporate existence and reasonable reliance thereon, does not exist. All the elements of any ordinary case of estoppel must be present to have a corporation by estoppel. The association must have been dealt with as a corporation and as such alone, to create an estoppel to deny corporate existence.

---

[17] *Mason vs. Nichols,* 22 Wis. 360.
[18] *Congregational Society vs. Perry,* 53 Wis. 316.
[19] *Witney vs. Robinson,* see note 6, *supra.*
[20] *Marshall on Private Corporations*—Page 134.
[21] 15 *Wend.* (N. Y.) 314.

Estoppel to deny corporate existence can arise in the pleadings of a case. A defendant who pleads a counterclaim in an action by a corporation, is estopped to deny the plaintiff's corporate existence.[22] The doctrine of estoppel to deny corporate existence applies to foreign as well as to domestic corporations.[23]

The state alone can attack the corporate existence of a corporation, de facto.[24] A corporation by estoppel exists, of course, only as against the person who deals with it as such and against him alone can it set up its corporate existence. The state could then, without question, institute quo warranto proceedings against such a pretended corporation.[25]

The doctrine of estoppel to deny corporate existence by reason of having contracted with an association as a corporation, is not limited to contracts between a corporation and strangers but applies also, in the case of contracts between such association and its stockholders or members.[26]

To sum up it can be said, that estoppel to deny corporate existence can arise without the presence of a de facto corporation, and having so arisen, such corporation by estoppel possesses all the benefits of a de facto corporation without being subjected to any of its requirements. Such corporation by estoppel, has no real existence in law, as has a de facto corporation, but is a mere fiction, existing for the particular case, and vanishing where the elements of estoppel are absent. A de facto corporation can exist forever as a de jure corporation, if the state does not interfere, but a corporation by estoppel must always look to the presence of the estoppel without which it is no more than an association of individuals, a partnership.

DAVID CHARNESS, 1922.

---

[22] *Black River Improvement Co vs. Holway*, 85 Wis. 344.
[23] 15 Cal. 679 and 21 N. Y. 542.
[24] *Farewell vs. Wolf*, 96 Wis. 10.
[25] *Marshall on Private Corporations*, 142.
[26] *Gilman vs. Druse*, 111 Wis. 400.