Corporate Resolutions in Leasing Transactions

By Thomas E. McCurnin

Although some transaction lawyers consider a corporate resolution to be an optional document, recent case law in New York, California, and Illinois compels the contract drafter to obtain this essential piece of paper for corporations, limited liability companies (LLCs) and limited liability partnerships (LLPs). Indeed, the lessor's lease, security interest, and any accompanying guaranties may become unenforceable if this crucial, yet simple, one-page document is not obtained.

CORPORATE RESOLUTIONS IN HISTORY

The doctrine of obtaining the "bona fides" of authority originates with the English monarchs of the 13th century. In ancient England, the royal seal was source of all power to issue decries and orders, and if a king was under attack and had to flee, the royal seal was probably the only piece of personal property that the monarch would grab, save and except his clothes.[1]

The requirement that contracts be signed under seal was brought to the United States and became a part of most state law. It was often a requirement for corporate documents, conveyances, stock certificates, and contracts.[2] Even though some states still cling to their use,[3] most states have eliminated the requirement of corporate seals altogether under the equal dignity rule,[4] and their presence generally has no effect on the document,[5] except for purposes of authentication.[6] One of the reasons for eliminating the use of the corporate seal was the fact that many states have longer statutes of limitations for documents signed under seal, sometimes as long as 20 years.[7] Thus, by affixing a simple corporate seal to a contract or corporate resolution, the corporation could be subjecting itself to the increased risk of an exaggerated statute of limitations.[8]

In the United States, the common law has developed three types of corporate authority: presumptive authority (by following strict guidelines in common law or by statute); actual authority (by a specific grant of authority in the bylaws or by a corporate resolution); and implied authority (authority implied by law by the officer's position and responsibilities).

If an equipment lessor wants its lease to be enforceable, then it should strive to obtain presumptive authority, if allowed within the state where the lease is being enforced. Otherwise the lessor should obtain evidence of actual authority.

SAFE HARBOR: PRESUMPTIVE AUTHORITY

California and Pennsylvania have simplified the nature of corporate authority and have created a safe-harbor statute for creditors, if the creditor follows certain statutory formalities. If at least two officers sign the contract, one in the executive position (president, vice president, CEO) and a second in the financial position (secretary, treasurer, CFO), then the law provides that there is presumptive authority to execute the contract. The presumptive authority can be obtained by either the contract being signed by the two officers, or by virtue of a corporate resolution signed by the two officers. Thus, no corporate resolution is needed, if the contract is signed by the two officers.[9]

A properly signed contract provides proof of authority. A contract signed in this fashion is not only presumptively authorized by the officers; the presumption is a nonrebuttable conclusive presumption, requiring no other proof.[10] Of course, if the creditor knowingly participates in a fraud with the corporate officers, the corporation will not be bound, because no officer has authority to defraud the corporation.[11]

Without a corporate resolution, the lessor's lease, security interest, and any accompanying guaranties may become unenforceable. If the lessor fails to secure the necessary evidence of corporate authority, the lessor will not be sealing the deal, but sealing its fate.

Most states do not have a safe-harbor statute and instead follow the New York rule that creditors dealing with the officers of a corporation are chargeable with notice of the authority, actual or apparent, of the debtor's officers or agents with whom they deal.

The states that still subscribe to the use of corporate seals may give presumption of authority for documents signed under seal.[12]

CORPORATE RESOLUTIONS: ACTUAL AUTHORITY

Most states do not have a safe-harbor statute and instead follow the New York rule that creditors dealing with the officers of a corporation are chargeable with notice of the authority, actual or apparent, of the debtor's officers or agents with whom they deal.[13] This puts the creditor at risk, and the creditor must assure itself that the person it is doing business with does, in fact, have the authority to enter into the transaction.

Merely holding a senior officer position in the corporation does not, in and of itself, cloak the officer with any inherent authority to sign contracts.[14] In many states, even a contract signed by the president of the corporation must be signed under seal, or authorized by a corporate resolution.[15] However, in other states, the president has statutory authority to sign contracts without a resolution,[16] except where the articles of incorporation prohibit the president from entering into contracts without consent.[17] In short, if the lessee resides in one of the states with presumptive authority, such as New Hampshire or Minnesota, simply having the CEO as a signatory may suffice to establish corporate authority, and in New York or Illinois may establish implied authority.

Because the laws of the states vary so much in this regard, the creditor must satisfy itself that the officer signing the contract has the specific authority to sign the contract. This can be done in either of two ways: by obtaining a corporate resolution or by examining the company's bylaws to determine whether the particular officer has the requisite authority to sign the contract.

Reviewing the bylaws is not particularly convenient, and only in the instance of a limited liability company would such a review be necessary. Therefore, most creditors satisfy this requirement by obtaining a corporate resolution.

LACK OF A CORPORATE RESOLUTION: PROVING IMPLIED AUTHORITY

Even if the creditor failed to obtain a corporate resolution, it becomes an uphill battle to establish corporate authority. In California and Florida, the creditor can establish implied authority by proving the following elements:

1. The person dealing with the agent must do so with belief in the agent's authority and this belief must be a reasonable one;

2. Such belief must be generated by some act or neglect of the principal sought to be charged; and

3. The third person, in relying on the agent's apparent authority, must not be guilty of negligence.[18]

These elements put the creditor on the defensive, because establishing implied authority, in the absence of a specific grant of authority, will be difficult. Moreover, the grant of implied or ostensible authority must be generated from some action of the principal. Often it is only the agent that cloaks himself with authority, and the principal has little or nothing to do with causing the creditor to believe that the officer or agent had authority to sign the contract.[19] However, if the corporation knowingly places an officer in charge of negotiating a transaction, it will be difficult for the corporation to later deny the officer had no authority to complete it.[20]

However, if a creditor is faced with the lack of presumptive or actual authority and is forced to prove corporate authority on the part of the officer in court, the creditor should examine the bylaws and determine whether the officer had the authority to sign contracts or leases. In addition, the creditor should also obtain copies of other contracts and leases the company entered into over the past few years to determine if the officer in question ever signed similar contracts. The majority rule in most states is that the prior grant of similar authority is evidence of authority for the questioned transaction, especially if the corporation acquiesced to prior unauthorized

actions.[21] However, in other states the past conduct must have been relied upon by the actual creditor in the present transaction to establish ostensible authority.[22]

Both New York and Illinois provide for implied authority if the officer is very senior, like a CEO or president, and the contract is for customary or necessary activities of the corporation. Thus, if the creditor is dealing with a very senior officer and the purpose of the contract is for supplying inventory or necessary services for the corporation, courts in New York and Illinois may protect the creditor in those states, even without a corporate resolution.[23] It would seem logical to assume that most leases would be for "customary or necessary activities" of the corporation, except in extreme circumstances. This author could find no indication that the size of the lease matters, but certainly a lessee could argue that a $50,000 small-ticket phone system should be treated differently from a $2 million machine tool product line or a luxury car for one of the officers.

If the creditor is unable to establish that the officer historically had authority to sign contracts, the creditor should determine if the debtor corporation knew about the contract and somehow knowingly authorized the contract, knowingly paid the lease payment for it, or accepted the benefits of the contract. If established, this may prove ratification of the contract or lease in most states, including both New York and California.[24]

SPECIAL RULES FOR LLCs AND PARTNERSHIPS

Limited Liability Companies

Limited liability companies do not have officers, directors, and shareholders per se; rather, LLCs have members.[25] The members that the creditor is dealing with may, or may not, have authority to sign contracts. There are two ways the creditor may be assured of establishing corporate authority when faced with an LLC member.

First, many states have a similar safe-harbor statute, allowing the creditor to deal directly with any LLC member as well as imposing a presumption of authority of that member, unless the lack of authority is stated in the articles of organization and the creditor had knowledge of the lack of authority.[26] However, this safe-harbor rule is on a state-by-state basis: absent a specific statute authorizing the creditor to deal with a single LLC member, the creditor may be at risk in doing so.

Second, the creditor may examine the LLC operating agreement for the LLC to see if one of the members has been appointed as "managing member," and to review the authority vested in that member.[27] In some states there may be confusion as to whether the document is in fact an operating agreement, as it may bear a title that is different from an "operating agreement."[28]

Third, if there is no operating agreement (none is required by most states), then the creditor must obtain either a corporate resolution with all the members signing the resolution in Illinois or New York.[29] Many banks and financial institutions have the LCC members sign a deposit agreement, which confirms the number of members as well as authorizes certain persons to sign checks and to negotiate with the bank. This deposit agreement also provides that none of the members will have its authority removed without notice to the bank, which ensures that the bank can continue to deal with the members and accept checks signed and endorsed by those members listed in the deposit agreement. The courts have upheld this type of agreement to establish both past and continuing authority of the members of the LLC, allowing the banks to rely on the agreement, even in the face of a corporate dispute where a member had its authority revoked.[30]

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Partnerships

With the advent of LLCs, partnerships are a rare entity these days, but the same rules apply. Either the creditor must review the partnership agreement to determine if the managing partner has authority to sign the contract, or a resolution of all the partners must be obtained.

EFFECT OF LACK OF AUTHORITY ON GUARANTIES AND COLLATERAL

It is a fundamental rule of law in New York and California that a guarantor's liability may be no greater than the liability of the principal,[31] which is generally measured at the time the documents are entered into. Therefore, if the lessee establishes that the lease was entered into without corporate authority, a strong argument can be made in those states that any guaranty the lessor obtained is void by operation of law.[32]

To add insult to injury, because the lease generally has the only grant of a security interest in the credit documents, the lessor may also lose its security interest in the collateral in the event of a successful claim of lack of authority.[33] Although the lessor may prevail on an equitable theory as against the lessee,[34] it would have little ammunition against a bankruptcy trustee for the lessee who asserts lack of authority as a defense.

Therefore it behooves the lessor to faithfully obtain the requisite documents to evidence corporate authority if it wants to enforce the lease, salvage its collateral, and enforce the personal guaranties.

CONCLUSION

Sometimes it seems that in small- and middle-ticket leases, corporate resolutions are an afterthought in the documentation process. However, the failure to obtain evidence of corporate authority may sink the equipment lessor's ability to enforce the lease. Although the lessor may be able to rely upon the inherent authority of the title of the officer who signed the lease, the fact that the lease was entered into in the ordinary course of business for routine and customary purposes, the lease is relatively small, the lessee ratified the lease with payments, or the officer previously entered into similar transactions without objection by the corporation, it does not seem wise to forgo what should be an essential part of any suite of lease documentation: the corporate resolution.

If the equipment lessor fails to secure the necessary evidence of corporate authority, the lessor will not be sealing the deal, but sealing its fate.

Endnotes

[1]Each king would design his own seal and no document was valid without it. Indeed, the Magna Carta contains both the signature and the great seal of King John. Documents were often merely sealed, not signed. The Great Charter of Canada, given by King Charles II to the Hudson Bay Company in 1670, was never signed by King Charles but was sealed. The authority of the king to make this historic grant to a private company was hotly contested in Canada and in British courts, but because of the existence of the seal the grant was held valid.

[2]*Rouse Teachers Properties Inc. v. Maryland Cas. Co.*, 358 Md. 575, 585, 750 A.2d 1281, 1286 (Ct.App. 2000). This case has an excellent history of the use of corporate seals in America.

[3]*Ward v. City of Cairo*, 276 Ga. 391, 394, 583 S.E.2d 821, 824 (2003) (rebuttable presumption); *Milford Fertilizer Co. v. Hopkins*, 807 A.2d 580, 583 (2002) (presumption); *Flo Control Inc. v. Northeast Bank*, 150 Ga.App. 880, 882, 258 S.E.2d 695, 697 (Ct. App. 1979) (Once seal is presented, document is binding on the corporation, even if forged); *Anderson v. City of Rolling Meadows*, 10 Ill.2d 54, 59, 139 N.E.2d 199, 201 (1957); New York Business Corporations Law Sec. 107, 202 (Corporate seal is allowed, but its use has no legal effect).

[4]*Rohm & Haas Co. v. Gainesville Paint & Supply Co.*, 225 Ga.App. 441, 442, 483 S.E.2d 888, 891 (Ct. App. 1997).

[5]California Corporations Code Sec. 313; 15 Pennsylvania Statutes Sec. 2852 305; *Moss v. Elan Memorial Park Corp.*, 400 Pa.Super. 555, 560, 583 A.2d 1254, 1257 (1990); McKinney's Consolidated Laws of New York, General Construction Law Sec. 44-a and comments thereto.

[6]McKinney's Consolidated Laws of New York, General Construction Law Sec. 44-a and comments thereto.

[7]McKinney's Consolidated Laws of New York, Civil Practice Act Sec. 47-b (20 year statute of limitations); Florida Statutes Sec. 95.11(1), Florida Statutes (1973) (now rescinded).

[8]*Republic Contracting Corp. v. South Carolina Dept. of Highways and Public Transp.,* 332 S.C. 197, 206, 503 S.E.2d 761, 766 (Ct. App. 1998); *Tipton v. Partner's Management Co.,* 364 Md. 419, 426, 773 A.2d 488, 492 (Ct. App. 2001); *Beneficial Consumer Discount v. Dailey*, 434 Pa.Super. 636, 637, 644 A.2d 789, 789 (1994).

[9]California Corporations Code Sec. 313; 15 Pennsylvania Statutes Sec. 2852 305.

[10]*Snukal v. Flightways Manufacturing Inc.,* 23 Cal.4th 754, 779 (2000; provides a conclusive rather than a merely rebuttable evidentiary presumption). *Saks v. Charity Mission Baptist Church*, 90 Cal.App.4th 1116, 1141, 110 Cal.Rptr.2d 45, 65 (2001).

[11]*Saks v. Charity Mission Baptist Church*, 90 Cal. App.4th 1116, 1138, 110 Cal.Rptr.2d 45, 65 (2001); Clarence L. Martin, P.C. v. Chatham County Tax Com'r, 258 Ga.App. 349, 574 S.E.2d 407 (2002).

[12]*Ward v. City of Cairo*, 276 Ga. 391, 394, 583 S.E.2d 821, 824 (2003) (rebuttable presumption); *Milford Fertilizer Co. v. Hopkins*, 807 A.2d 580, 583 (2002) (presumption); *Flo Control Inc. v. Northeast Bank*, 150 Ga.App. 880, 882, 258 S.E.2d 695, 697 (Ct. App. 1979) (Once seal is presented, document is binding on the corporation, even if forged); *Anderson v. City of Rolling Meadows*, 10 Ill.2d 54, 59, 139 N.E.2d 199, 201 (1957).

[13]*Thompson v. Marseillaise French Baking Co.,* 85 Misc. 392, 394, 147 N.Y.S. 402, 403, 85 Misc. 392, 395, 147 N.Y.S. 402, 403 (1914); *In re Union City Milk Co.,* 329 Mich. 506, 512, 46 N.W.2d 361, 364 (1951).

[14]*Hudson United Bank v. Cinnamon Ridge Corp.,* 81 Conn.App. 557, 573, 845 A.2d 417, 430 (2004); *Computer Maintenance Corp. v. Tilley*, 172 Ga. App. 220, 322 S.E.2d 533 (1984); *Orphan Aid Soc. v. Jenkins*, 294 S.C. 106, 109, 362 S.E.2d 885, 887 (Ct. App. 1987); *Brand v. Lowther,* 168 W.Va. 726, 735, 285 S.E.2d 474, 481 (Ct. App. 1981); *Electronic Development Co. v. Robson*, 148 Neb. 526, 535, 28 N.W.2d 130, 136 (1947).

[15]*Computer Maintenance Corp. v. Tilley*, 172 Ga.App. 220, 222, 322 S.E.2d 533, 536 (1984).

[16]*Chisholm v. Ultima Nashua Indus. Corp.,* 150 N.H. 141, 146, 834 A.2d 221, 226 (2003); See Minn.Stat. Sec. 302A.305, subd. 2(d) (2002) (recognizing authority of chief executive officer to sign and deliver contracts in the name of the corporation).

[17]*Breaux v. Lafourche Parish Council*, 851 So.2d 1173, 1175 (La.Ct. App. 2003).

[18]*Keppelman v Heikes*, 11 Cal.App.2d 475 (1952); *Singer v. Star,* 510 So.2d 637, 640 (Fl.Ct.App. 1987).

[19]*Mesce v. Automobile Ass'n of N. J.,* 8 N.J.Super. 130, 135 73 A.2d 586, 588 (1951); *Taco Bell of California v. Zappone*, 324 So.2d 121, 123 (Fla. Ct.App. 1976); *Beasley v. Kerr McGee Chemical Corp.,* 273 S.C. 523, 257 S.E.2d 726 (1979).

[20]*AutoXchange.com Inc. v. Dreyer and Reinbold Inc.,* 816 N.E.2d 40, 49 (Ind. Ct. App. 2004).

[21]*Preis v. American Indemnity Co.,* 220 Cal.App.3d 752, 761 (1990); *Snukal v. Flightways Mfg. Inc.,* 23 Cal.4th 754, 779, 3 P.3d 286, 305, 98 Cal.Rptr.2d 1, 22 (2000); *Fontenot v. Aetna Ins. Co.,* 225 So.2d 648, 652 (La. Ct. App. 1969); *O'Neal v. Crumpton Builders Inc.* Excerpt from: 143 So.2d 344, 345 (Fla. Ct. App. 1962); *T.S. McShane Co. v. Great Lakes Pipe Line Co.,* 156 Neb. 766, 773, 57 N.W.2d 778, 782 (1953); *Terry Square Motors v. Haber,* 137 Conn. 377, 379, 78 A.2d 337, 338 (1951).

[22]*Kiniski v. Archway Motel Inc.,* 21 Wash.App. 555, 563, 586 P.2d 502, 508 (1978) *Carpenter v. Payette Valley Co op. Inc.,* 99 Idaho 143, 146, 578 P.2d 1074, 1077 (1978).

[23]*Goldenberg v. Bartell Broadcasting Corp.,* 262 N.Y.S.2d 274 (1965); *Smith v. Shoreline Printers & Publishers Inc.,* 6 Ill.App.2d 290, 295 (1955).

[24]California Civil Code Sec. 2310; *Standard Funding Corp. v. Lewitt*, 89 N.Y.2d 546, 678 N.E.2d 874, 656 N.Y.S.2d 188 (1997).

[25]California Corporations Code Sec. 17001(d); McKinney's Limited Liability Company Law Sec. 401.

[26]Utah Revised Limited Liability Company Act Sec. 48-2c-802; McKinney Limited Liability Company Law Sec. 412; California Corporations Code Sec.17157.

[27]McKinney's Limited Liability Company Law Sec. 401.

[28]In New York, the definitions to the Limited Liability Company Law (LLCL Sec. 102[u] and see LLCL Sec. 417) state that an operating agreement is a written agreement of the members. It must be signed by all the members. *Spires v. Casterline,* 4 Misc.3d 428, 434, 778 N.Y.S.2d 259, 264 (2004).

[29]Illinois Statutes Ch. 805 Sec. 180/13-5.

[30]Innovare Logistics, *LLC v. Parish Nat. Bank,* 890 So.2d 643, 644 (La Ct.App. 2004).

[31]Civil Code Sec. 2809; *Eckstein v. Mass. Bonding & Ins. Co.,* 281 N.Y. 435, 24 N.E.2d 114.

[32]*Bloom v. Bender,* 48 Cal.2d 793, 802, 313 P.2d 568, 573 (1957); *Eckstein v. Mass. Bonding & Ins. Co,* 281 N.Y. 435, 24 N.E.2d 114 (1939). The rule originated from the Napoleonic Code. This defense may be waived, and this waiver is generally found in most guaranties, but unlikely to be included in the one paragraph guaranties found within equipment leases in the small- or middle-market ticket leases.

[33]The new Article 9 to the Uniform Commercial Code requires that the security agreement be "authenticated," Sec.9-203(b)(3)(A), which by definition includes being authorized by the debtor.

[34]Warren Tool Co. v. Stephenson, 11 Mich.App. 274, 161 N.W.2d 133 (1968) (Equitable liens retain vitality despite enactment of Uniform Commercial Code).

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