

Continental Hotels, Inc. v. Koror Travel Services, 1 ROP Intrm. 306 (1986)

**CONTINENTAL HOTELS, INC.,
Plaintiff/Appellee,**

v.

**KOROR TRAVEL SERVICES,
Defendant/Appellant.**

CIVIL APPEAL NO. 2-84
Civil Action No. 206-84

Supreme Court, Appellate Division
Republic of Palau

Opinion

Decided: April 11, 1986

Counsel for Appellant: Kaleb Udui

Counsel for Appellee: Kevin Kirk

BEFORE: MAMORU NAKAMURA, Chief Justice; LOREN A. SUTTON, Associate Justice; and PAUL J. ABBATE, Part-time Associate Justice.

NAKAMURA, Justice.

I.

In 1974, a Mr. Minoru Ueki and Mr. Masami Asanuma were instrumental in organizing a business enterprise named Koror Travel Services (“KTS”). Under the Articles of Incorporation, By-Laws and affidavit, Ueki, Asanuma and Mr. Ngiraingas Oiterong were named as members of the Board of Directors and officers of the company. The three individuals were also named as subscribers to 500 shares of KTS corporate stock. A corporate charter was issued to KTS, but the stock subscriptions were neither called for nor received by the corporation. The law of the Republic of Palau requires paid-in-capital of \$1,000 before a domestic corporation can conduct business. ROP Corp. Regs., Title 37, Pt. II, par. 2.7. KTS did not comply with this requirement until September 1981.

The idea to form KTS derives from a Japanese national named Takayuki Yamamoto who suggested that Ueki assist him in forming a tourist business in Palau. The understanding was **¶307** that KTS would operate a tourist business in Palau while Yamamoto would advertise and make arrangements for Japanese tourists to visit Palau. Yamamoto would collect payment from the tourists in Japan and then pay KTS for catering and serving the tourists who visited the island through Yamamoto’s sponsorship.

Pursuant to this arrangement and after the formation of KTS, Yamamoto operated a

Continental Hotels, Inc. v. Koror Travel Services, 1 ROP Intrm. 306 (1986) tourist business in Palau under the KTS name. (KTS officers and directors were aware of Yamamoto's use of the KTS name). Yamamoto obtained the assets necessary to conduct a tourist business, such as buses and boats. These assets were registered in the KTS name and some had the Corporation's name printed on them. The officers and directors of KTS, mainly Ueki and Asanuma, provided assistance to Yamamoto by obtaining entry permits and providing language translation when necessary. Moreover, Asanuma Enterprises, an entity operated by Asanuma's family, provided office space for KTS. Yamamoto, using the KTS name, entered into arrangements with Continental Hotels, Inc., which operated the Palau Continental Hotel located in Koror. This arrangement provided KTS with an open credit account. In addition to Yamamoto, Continental conducted business with KTS through Mr. Yukio Moriyama. The KTS officers and directors were aware of these arrangements.

In 1980 and 1981, Continental Hotels accumulated uncollected bills of over \$14,000 chargeable to KTS. In June 1981, Continental Hotels stopped accepting charges to the KTS account. At that time, Yamamoto began operating another tourist business in Palau named Belau Tour Agency. Also, in June 1981, Asanuma Enterprises and other third parties took over KTS and performed the statutory requirements necessary for KTS to conduct business in Palau.

II.

Continental Hotels filed suit against KTS for collection of the outstanding debt. KTS defended alleging it lacked corporate existence prior to September 1981 and therefore could not be liable for debts accumulated in its name by Moriyama and Yamamoto. The trial court held: 1) KTS as a de facto corporation from 1974 until 1981, even though it had not received the paid-in capital for the stock subscriptions; and 2) KTS was liable for the debts incurred in its name as the debts of the "old" corporation inured to the "new" corporation. KTS appealed.

1308 III.

On appeal KTS argues that the failure to comply with Title 37, Part II, Paragraph 2.7 of the Palau Corporate Regulations prevented it from having a corporate existence from 1974 until September 1981. KTS contends that its lack of corporate existence precludes it from being liable for the debts incurred in its name. Alternatively, KTS asserts that the assignment of subscription rights by the original subscribers did not transfer the liabilities of KTS, if any.

Continental Hotel replies to the arguments made on appeal by KTS by arguing that KTS' actions met the elements necessary to establish a de facto corporation. Additionally, Continental asserts that the individuals who incurred debts in KTS' name were the agents of KTS, thereby rendering KTS liable for such debts.

The following issues are raised by this appeal:

- 1) Whether KTS lacked corporate existence from 1974 to 1981 due to its failure to comply with the statutory requirement of receiving a minimum amount of paid-in capital prior to conducting business; and

- 2) Whether KTS is liable for the debts accumulated in favor of Continental Hotels in 1980 and 1981 resulting from business transactions with persons acting in the name of KTS?

IV.

KTS argues that its failure to comply with the statutory capitalization requirement deprives it of corporate existence and renders it incapable of incurring debts. The trial court correctly rejected this argument concluding that KTS was properly considered a de facto corporation. A corporation without valid legal existence may nonetheless have corporation status in fact where the following elements are present: 1) the existence of a law under which the entity may validly incorporate, 2) a colorable attempt on the part of the corporation to comply with the law, and 3) some use or exercise of the corporate privileges. *Tulare Irrigation District v. Shepard*, 185 U.S. 1, 13, 22 S.Ct. 531 (1902). That facts amply demonstrate KTS' de facto existence. That there is a statute allowing incorporation is not disputed. Nor is there any question that KTS took advantage of corporate privileges by incurring debts in the name of the Corporation. KTS contends, rather, that its failure to properly capitalize prevents a §1309 finding of colorable compliance. This argument is not persuasive for two reasons. First, there is evidence of substantial compliance. Articles of incorporation were created and by-laws duly promulgated. The corporation named directors and elected officers. A corporate charter was issued and stock subscribers identified. The failure to call for and receive the stock subscriptions was perhaps the only remaining act before the corporation obtained de jure status. The trial court was correct to find colorable compliance.

Second, and of more significance, under principles of equity, KTS, having held itself out of the public as a corporation and having incurred debts in its corporate name is now estopped from denying its corporate existence. An entity holding itself out as a corporation and conducting business as such is estopped from denying its corporate existence in an action brought against it. *United States v. Theodore*, 479 F.2d (4th Cir. 1973); *see also, e.g., Watwood v. Barber*, 70 F.R.D. 1 (N.D. Ga. 1976) (person who held themselves out as a corporation and do business as such cannot set up lack of legal incorporation to escape liability in an action against the corporation); *Wynn v. Treasure Co.*, 146 C.A.2d 69 (1957) (a person who has acted as a director, officer, or agent of an entity purporting to be a corporation is estopped from denying its corporate existence). See generally, N. Lattin, Lattin on Corporation, 166-168 (1959). Accordingly, we agree with the trial division that Koror Travel Services cannot, in this action, deny its corporate existence.

There is also raised an issue as to whether the debts in favor of Continental Hotels were properly incurred in the corporate name. The facts establish that KTS entered into a contractual relationship with Moriyama and Yamamoto. The two men acted as agents of the corporation carrying out the corporate business, both in Palau and Japan, under the KTS name. KTS now claims that the debts incurred by the agents in favor of Continental were unauthorized acts creating no liability on the part of the corporation. We agree with the trial court that the corporation cannot now disaffirm the authority. The unauthorized act of an agent, purportedly

Continental Hotels, Inc. v. Koror Travel Services, 1 ROP Intrm. 306 (1986) done for the benefit of a principal, can be subsequently ratified by the principal by implication through conduct which is inconsistent with an intention to repudiate. *Weber v. Towner County*, 565 F.2d 1001, 1008-1008 (8th Cir. 1977). Here, the corporation, fully aware of the Continental account, did not take any action to notify Continental of purportedly unauthorized acts, nor otherwise move to disaffirm the acts of the agents; such conduct will properly imply ratification. Moreover, KTS continued to accept the fruits of the agency §310 relationship. Under the law of agency, a principal cannot disaffirm the authority of his agent to make a contract and at the same time retain the benefit of the unauthorized acts. *Id.*; *McDonald v. Hamilton Electric Inc. of Florida*, 666 F.2d 509, cert. denied, 459 U.S. 879 (1982). The actions and inactions of KTS precludes it from now denying liability for debts incurred by its agents.

Were these debts assumed by the “new” KTS corporation under the 1981 stock assignment? We agree with the trial court that the debts were so assumed.

The subsequent compliance with the requirements for doing business did not create a new corporation. Instead, it was a continuation of the old corporation. See *Bishop v. Dura-Life Manufacturing Co.*, 489 F.2d 710. *Diamond A. Cattle Co., v. Tshirgi*, 181 F.2d 991 (10th Cir. 1950); *Consolidated Electric Cooperative v. Panhandle Eastern Pipeline Co.*, 189 F.2d 777 (8th Cir. 1951). Assuming compliance with the statutory requirements created a new KTS corporation, such a corporation would still be liable to Continental Hotels on the basis of fraud.

Continental Hotels stopped extending credits to KTS in June 1981. In June 1981, the original stock subscribers assigned their subscription rights to new shareholders with, Asanuma, one of the original subscribers, being directly or indirectly connected with Asanuma Enterprises. To rule that KTS bore no liability to Continental would, in effect, uphold a fraud upon Continental Hotels. See *Forest Laboratories, Inc., v. Pillsbury Co.*, 452 F.2d 621 (1971).

The trial court decision is affirmed.