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## I.—*The Joint-Stock Companies in the Court of Equity.* By F. R. Falkiner, Esq., Q.C.

[Read Tuesday, 8th June, 1869.]

EVEN a superficial eye-witness of the last fourteen years' litigation at Westminster and Dublin is startled to see the position held in our Courts of Equity by the joint-stock companies. The proportion of judicial attention they have engrossed, as compared with any other single object of equity jurisprudence, is stupendous. It may be seen by taking at random any volume of the Chancery Reports published in those years, and looking in the index at the titles—"Public Company;" "Contributing;" "Winding up." The equitable windlass has wrought incessantly, and as the bystander watches this moving machinery, passing strange are the dissolving views of folly, fraud, and recklessness unrolled before him. Limited companies got up by impudence unlimited, acting on credulity as boundless, and adjourned from the counting house to the Chancery with startling speed; fraud, folly, failure following each other in very wondrous yet very natural succession. Wise men and fools, strong men and weak, alike seized, drawn in, and wound up by the inexorable engine of contribution—are not those things written at large in the chronicles of our courts of equity for the last fourteen years? What most surprises one, looking wistfully at all this, is the number of the wise and the strong to be seen amongst the victims. Truly the knights of industry have been errant and active in the land, but it is not witless maids nor moon-struck youths they have beguiled with their romances. The hard-headed, the hard-fisted, I was about to say hard-hearted, have softened to their tales of wonderment and fiction. Seriously, wary men of the world, prosaic and thrifty, who

in their private outlays were supposed to have never spent an unnecessary shilling; who, investing on mortgage, would as soon give £1,000 away as lend it without the opinion of a conveyancer, or take the risk of the most fanciful flaw in title, pour out their thousands in unquerying faith to the painted falsehoods of an anonymous prospectus, or on the bill of exchange of a company which the youngest lawyer would tell them was *ultra vires* of the corporation, and waste paper. There are many weak points in our joint-stock systems discovered by equitable diagnosis, which I do not intend even to touch upon. That doctrine of *ultra vires* for instance—I mean the application of the rules of equity to the unauthorized acts of directors—discloses a list of complex difficulties which have not yet been solved. I confine myself to some reflections suggested by the aspect in court of certain financial flagrancies, which I cannot but attribute to the misuse made of the limited liability statutes. Premising, too, that I speak from a point of view admittedly partial and inadequate, as a lawyer who has seen a part, and not as an economist who has explored the whole. I do not at all know the statistics of this question—what the proportion of the companies that have failed to those which have succeeded. I fear therefore lest I may generalize too far.

My desire this evening is to present in panorama a few pictures that have already passed before the spectator in the Court of Chancery; then to point out some innate vices in the principles on which the companies so seen were founded; to consider how far the law pretends, and how far it does not, to deal with those disorders; and finally, with considerable self-distrust, to suggest certain legislative remedies, drawn as far as possible from the stores of established principle, and therefore savouring rather of old custom than of innovation.

I have intentionally selected for examples a few average specimens of cases dealing with concerns of average magnitude, purposely avoiding the great crashes, whose bursted bubbles have caused a shock in the commercial atmosphere of the empire, and whose ill-fame has unpleasantly perfumed society. The big cases, though more dramatic, are, I think, scarcely as instructive as the more moderate examples. I fear the exceptional magnitude which makes them sensational may induce in many a confused inference that their evils are exceptional also. If radical infirmities which caused their dissolution exist also in the average undertakings, it indicates, I think, a more subtle, because a less noticeable danger, and the lesson from noticing it is therefore more worth the learning. So I pass by Overend, Gurney, and Co., and Barnard's Bank, and the like, whose victims show fresh wounds to the world in the morning papers, and have so often pointed the moral of *ex post facto* philosophers in leading articles.

An instance commercially small, but illustratingly striking, in which I was professionally engaged, first set me thinking on this subject. A young gentleman came over here from England, he entered Trinity College, and at the same time into a contract for the purchase of a handsome demesne in this county. He found a piece of land

adjoining an old disused copper mine, and for a few pounds obtained a lease and license to work it. It was sworn in the case by a mining engineer that, employed by this young gentleman to examine the field, he inspected it, and reported it to his employer as wholly worth less But though a place where ore was not to be won by iron, this speculator found it a mine whence gold might be won by brass, and he proceeded as follows. He made it, like the Potter's field, a place to bury strangers in. He sent through the north of England, notably to monied Manchester, a flaming prospectus, handsomely it spoke of Ireland and her incarcerated treasures waiting for the sesame of English capital to unlock the caverns; specifically it spoke of the Potter's field; and lyingly of the splendid results of the experimental trials. Next he had drawn up a memorandum and articles of association, elaborately prepared to provide for centuries of successful mineral winning. The companies' act, 1862, provides that seven or more persons may form an incorporated company by subscribing a memorandum and articles of association, and registering these in the registry of joint-stock companies. Our promoter did not himself sign the memorandum and articles He nominated seven others less subtle than himself. Some of these were clerks whom he called into the room where the documents lay, and who then for the first time heard they were about to be incorporated by statute as owners of a mine hitherto unknown to them. I took the trouble of comparing the registered abodes of the seven incorporated ones with Thom's Directory, and found, I speak it seriously, the word "Ruins" as the residence of one; "Tenements" that of another; and "Model Lodging House" that of a third.

The articles of association provided that the first monies of the company coming to hand should be applied in completing a contract, theretofore made by two of the promoters, for the purchase of the Potter's field at £10,000, the vendor's name was not mentioned—it was of course our hero freshman. The two purchasers were two of his nominees—one the Secretary of the company, the other a gentleman who, after the crash, on oath in the Insolvent Court, stated his only assets in the world to be £100 *promised* him by our hero for his trouble in this transaction. Strange as it may appear, monied Manchester came in to this audacity. In a few weeks £4,000 were paid into the company's bankers, and drawn out by our hero's checks, countersigned by his nominees. In a few months more he ceased to develop the resources of this country; passed over to another, the bubble burst; monied Manchester rushed over to look after the plant, but found it consisted chiefly of the inexorable windlass; as for the ore, it was mythical as the gems in the garden of Aladdin. Not a director to be found; not a shilling of contribution from the promoters; no reality in the concern, save the expense of getting it up; unpaid accounts for sinking shafts and raising the wind, costs of working the equitable windlass, all which monied Manchester found real enough, having to meet them without the least assistance at this side of the channel. All else was a light-hearted little fiction. There is not the slightest exaggeration in the above, and yet I suppose people imagine Charles Dickens overdrew in his

immortal description of Mr Tigg Montague and the Anglo-Bengalee and Disinterested Loan Insurance Company. Yet Mr. Tigg had, at least, a grand piano to meet the coming crisis.

The case I have instanced was one of complete hollowness—having no substantiality of any kind; but it is the more remarkable on that account, as a sample of how far complete audacity can count on gullibility in these wise times. To be sure, the affair was not a large one, but I strongly think that had the freshman named his purchase money £50,000 instead of £10,000, he would have multiplied by five his victims and his gains.

I take next a case which the deciding judge expressly states he believed was not a bubble. In *Henderson* v. *Lalor* (L.R. 5, Equity, 249,) the plaintiff sought to be removed from the shareholders' list of the Great Yarmouth Hotel Company (Limited), on the ground that he was deceived in the statements of the prospectus, which gave as directors of the company the names of five gentlemen of position and respectability, and amongst other things alleged, "the directors and their friends have subscribed a large portion of the capital, and they now offer to the public the remaining shares" The qualification of these first directors was to be ten, and of future directors thirty shares. Wood, V.C., (now Lord Hatherley) in his scathing judgment thus describes the "getting up" of this affair—"They (the directors) are gentlemen whose names carry weight, and the plaintiff, who has been examined in court, says that on seeing the name of one of them, whose connexion with the town he well knew, and finding this was to be a hotel 'backed by him,' he thought its success was very fairly assured, coupled with the representation that the directors and their friends had subscribed a large portion of the capital. But instead of their having taken any shares at all, the whole transaction is this:—a man named Howe has made an affidavit, but he is not now to be found so as to admit of his being cross-examined, and therefore I have struck out his evidence, and I would rather not make any observation on his part of the transaction, except so far as he is connected with the position in which he has placed the defendants, the directors. This person I suppose is one of those who have taken upon themselves the name of 'financial agents' or something of that sort. He is an accountant. He seems to have been determined to concoct this company, and his mode was this: seeking first a set of directors, he goes into, as I once before had occasion to call it, 'the director market,' and there he finds these gentlemen, the defendants, and he tells them he wishes to make use of their names as directors of this company which he is about to project. They say, 'Very well, we will act as directors, but we will not, one of us, put a single sixpence into the concern. We will not act as directors unless our qualification be found for us.' The qualification is to be only ten shares. Howe contrived very ingeniously that the first directors to be appointed should only have to be qualified by ten shares, and that the subsequent directors must be qualified by thirty. His reason for doing this no doubt was that he saw there was very little chance of his being able to procure directors, unless he furnished them with their

qualification, and therefore his scheme was this: 'Let me have your names as directors. You shall have not one single farthing to lay out; I will furnish you with all the shares out of the money which shall be coming in from the intending subscribers. You shall have fully paid up shares, which will supply you with your qualification. I shall give you the paltry sum of £100 (*paltry* I mean with reference to the magnitude of such transactions as some of these are), taking care that I shall be paid £2,500 out of the first moneys coming in to the company (promotion money), and out of that I can buy you your shares.' So that the whole scheme of the company was this, that the directors were to have their shares found them by the future company. Now that does seem to me to be a very singular transaction for these gentlemen to engage in. The only consolation one has at looking at the case is this—I ought in justice to make the observation—that this does not appear to have been a bubble company. I look upon it as having been intended to be a *bonâ fide* one."

Mark in the above how the intern working partners, the directors, subscribe no capital, save what is all unconsciously supplied by the extra public partners, the unsuspicious shareholders; and how the former run no risk, for the liability is limited by statute to the amount of unpaid calls, and the shares of these gentlemen are all paid up.

Take next a company more real still, one which had a real property, of real workable value, which held place for a while in the world of trade and fact, and even paid some dividends. *Kent* v. *The Freehold Land and Brickmaking Investment Company* (L. R. 4, Eq, 588), in which Mr. Kent, a deluded shareholder, by a success reversed upon appeal, got a decree from Wood, V.C., disconnecting him with the company. I read from Lord Hatherley's judgment the following narrative: "The facts of the case are these. The defendant, Thomas Spargo, is minded to get up a company; with that view he looks first into the land market for some land, and buys about eight acres for £1,500; which was probably a tolerable price, it containing not otherwise than valuable brick earths. He then goes into the director market, and he buys six directors by giving them each £100, with a further engagement that each should have £100 a year, (that is £600 a year) for his labour. Having done that, he and the directors put their heads together to frame a prospectus, for there is no doubt the prospectus was framed by Spargo and assented to by the directors. He says so directly; they are not quite so frank, but they must be held answerable for the statements it contained. Then, having given £1,500 for the land, he makes a private arrangement with the directors or agents of the company (they having received the gratuity of £100 each and promise of £100 a year)—that the company should give him £6,250 for the land for which he had agreed to pay £1,500 himself. It is afterwards inserted in the articles of association that the directors are to pay the vendor out of the company's funds this £6,250, and a sum of £1,500 to Spargo as promotion money. That scheme being arranged, what do they tell the public? They say the capital is £25,000 in 5,000 shares of £5 each; they announce to the world the names of

the directors, Spargo not being one; they describe the land in somewhat glowing colours, but I will assume the description is not overstated; and go on to say the freehold has been purchased for £6,250, subject to a royalty of 2s. 6d. per 1,000 for bricks. That royalty was to be paid Spargo, in addition to the promotion money. It proceeds to say 'one half the desired capital has been subscribed by the directors and their friends,' and states that the land proprietor, Mr. T. Spencer, had taken 500 shares. It was he who had sold the land to Spargo for £1,500, and I must take him to be the man represented to have sold it for £6,250, because it says 'Mr. T. Spencer, the land proprietor, has taken 500 shares.'" His Honour, after referring to a statement in the prospectus that a dividend of 15 per cent. for fifteen years had been guaranteed, not mentioning that Mr. Spargo was the intended guarantor; to the fact that not one-fourth of the capital had been subscribed when the prospectus said one-half had been; decided there was ground for relief in the misrepresentation which made the purchase money £6,250, it being £1,500 in truth; adding, "the petitioner complains of having been misled by directors who have been bribed, and who paid this sum of money in consequence of having been so; Spargo having got up the whole scheme, and the directors having paid him."

Observe here how the relief is confined to the affirmative falsehoods, it nowise rests on the utter hollowness of the directory, and the concealment of that mockery. His Honour refused relief on the ground of the guaranty of 15 per cent, deciding that a shareholder promised such guaranty if he join is bound to find out its validity. I can see a regret underlying this judgment that authority and the system confine it within rather narrow limits, and even so it has been reversed, but altogether on grounds to which I shall have occasion to advert.

One other case in which there seems to be more reality still. Ross *v.* Estates Investment Company (L. R. 3, Eq. 122), also heard by Wood, V.C. The prospectus stated that the company had contracted to purchase the Selhurst Park estate at Norwood, on which it alleged £70,000 had been already expended by the *vendor*, and the Leytonstone estate, near London, the price of both to be £150,000, and alleging that half the first issue of 5,000 shares had been already subscribed, invited applications for the *remaining* shares. Not one word in this prospectus to tell that the head, and front, and sole substantial personality in this affair was one Mr. Lord, or that he was to have £10,000 promotion money for his trouble and ingenuity. I condense from the Vice-Chancellor's judgment this description: "Mr. Lord was not merely what is technically called a promoter (which means nothing more than a man who is to have a large bonus given to him for having struck out the idea of forming a company,) but he was in substance the promoter; as between him and the directors they looked upon him as the person who had the whole formation of the company, who was to pay all the expenses if it failed—the principal mover and author He had signed an agreement by which he subscribed for 2,510 shares (ten above the half), to be allotted him by the directors, in such manner as he might direct.

The representation in the prospectus that more than one half the shares had been already subscribed was printed in large type and in red ink at the head, evidently intended to have important weight with all who might apply for shares, and which, taken with the reference to the *remaining* shares, means that the directors have not 5,000 shares at their disposal, that 2,500 have been got rid of, and that the public must be quick and prompt or they will not be in time. The matter was in this position—if the thing broke down, Lord was under no risk at all, beyond paying £1,500 for the expenses of forming the company. He was to set it afloat, send it into the market, frame the prospectus, and see how people could be induced into the concern; and we find him pushing the 2,510 shares into the market, arranging that the public might believe they were bidding for the reserve 2,490, and that they could be allotted a valuable property, in which a large investment had been made, and on which £70,000 had been spent beyond the purchase money—a contrivance and advice (as to the shares) strict in the letter, but necessarily calculated, and obviously intended, to mislead and deceive those who might apply. *He* had not laid out one sixpence on the Selhurst estate, and as to the Leytonstone there was no binding contract; it was a mere speculation between himself and the vendor, contingent on the company being got up" And yet in the transactions there seems to have been this reality, that Mr. Lord had indeed contracted for the Selhurst estate; that former owners may have expended very large sums; and Mr. Lord was at least responsible to his confederate directors, up to £1,500, if the design should collapse.

Companies like those above described are defective in two directions, which I would keep apart. As commercial concerns they are formed on principles which render success scarcely possible; and as partnerships they are formed on principles most unjust as between the parties. I propose to consider these faultinesses separately, noticing how far the law, as it stands, connives at or remedies the existing evils, before venturing to suggest some alterations for which legislative sanction might not unreasonably be hoped.

As commercial undertakings they are constituted on principles which reverse the conditions once thought to be the without-nots of prosperity. Ninety-nine of every hundred men who, as individuals in trade, have made their fortunes, will tell you it was by the persistent supervision of their own business by their own selves—the persons indeed interested in its welfare or its failure, by cautious development of these undertakings as foresight with experience dictated; by using hirelings as little as might be, and their own services as far as possible; by reducing preliminary or unproductive expenditure to the minimum, and never dividing profits until they were gained; by allowing the business to develop the establishment, instead of taking chance for the establishment to develop the business. How many successful undertakings I should wish to know are there whose prosperity has not been solely represented by the personal labour and personal anxiety of the proprietors, and the saving of salaries resulting thereby. The success of all commercial enter-

prise depends on the manner in which capital is applied to industry. Capital and industry are not enough, they must be mutually adapted with foresight, economy, energy, and skill. Of the well-working machine wherein such adaptation exists, *self-interest* is the mainspring. For the application of that principle to the undertakings of partnerships and trading companies the rules of our common law, however otherwise questionable, were eminently favourable. Those rules compelled the persistent personal attention which ever at least deserves, and so most frequently commands, success; every shareholder being a partner, or liable, as the phrase went, to his last acre and last shilling, and so the solvency of the undertaking was of the last necessity for each. The business was therefore conducted by the parties themselves, or by certain of them delegated by the rest, not at haphazard, but after serious consideration, and was regulated upon the laws of human nature whereby individuals as well as firms prevail. Men whose would be the profit, and on whom would fall the loss, would not usually leave the fates and fortunes of their families and themselves to the transient solicitude of a financial agent.

Compare with the thrifty maxims which made rich our simpler fathers the laws, or rather the lawlessness, on which our modern joint-stock companies are so often based. The concerns started not where experienced wants have called for a supply, but where a speculative knave has ransacked selfish brains for an idea. The idea started not to be developed, but to be sold; not patiently tested by an originator interested in its successful growth, but purchased from an originator interested in its not being tested at all; profits anticipated months and years before they can be hoped for; reckless squandering upon preliminary expenses from which no profit is ever hoped at all; the thousands of pounds of the permanent proprietors handed over to those promoters whose anxieties cease with the promotion; the internal management of all things in the hands of nominal proprietors, the real proprietors without power or knowledge in the management; directors whose sole interest in the capital is the shares by which they have been bribed, further paid for a supervision they are *not* to give by fees taken from capital in further anticipation of profit, and the work which they do not do paid over again out of capital to salaried officials; the concern conducted by persons riskless in case of failure—for is not their liability limited to the "paid-up" shares they have taken as a gift; and by participation in the preliminary plunder, have they not interest direct in the state of things which make ruin almost inevitable? Is it wonderful if the real business of such co-partnerships commences in the Court of Chancery?

Do not suppose I mean an indiscriminate attack on the principles of limited liability. In a modified form it was a necessity to our commerce and our law. Indiscriminate limitation of liability I do assail. It alone makes possible the cohesion to such conspiracies of men of money and of mark. I cannot help thinking its present existence is one of those wrongs which the whirligig of time ever brings in to punish the anomalies of a fallacious law. Rules most wise in origin, falsely applied, cause confusions which throw doubt on their

original wisdom, and society, getting angry, abolishes the wise rule, not content with abolishing the foolish application. Nothing can be more just than that the ostensible active partners in a trading firm should be liable to the extent of their assets for the debts of the concern. Who would think of exacting that an individual trader should not in bankruptcy be liable to the limit of his means, and what are partnerships or joint-stock companies but aggregates of individuals? The salutary effect of unlimited responsibility I have already adverted to, but our common law, as interpreted for those questions, of a certainty went far further than the justice of the principle demanded. It was fair that those ostensible and active persons, on whose credit the public dealt with the firm, should meet the public credit to the uttermost, but the law made liable to the uttermost, side by side with working proprietors, the unnamed partner or the anonymous shareholder, whose interest in the concern might be little more than nominal, whose power over it was nil, and on faith of whose name no one could have credited the firm with a pound The doctrine went so far as to include in this iron responsibility creditors and even servants of the firm who were paid out of the profits. As this false doctrine grew and expanded, it caused injustices which roused a cry for its repeal. The false reasoning, both in point of economy and of jurisprudence, which induced so wild an expansion, was admirably exposed by Mr. Commissioner Fane before a committee of the House of Commons in 1851; his almost fiery evidence is printed in a note to Mr Linley's work on the Law of Partnership. I remember a cause tried at Belfast some time ago, in which, five years after the failure of a great Glasgow firm, an action for several thousand pounds of their bills of exchange was taken against a young man who had been their travelling clerk in the north of Ireland, founded on a clause in his agreement of hiring, which graduated his salary according to the profits. He had ceased all connexion with the firm for years before, on its failure, and had married and thriven in the interval, and I am by no means sure he would have escaped ruin, but that the House of Lords, shocked by the public opinion which now was growing into a storm, had shortly before, in the case of Cox *v.* Hickman, retracted some judicial views that hitherto had passed current, and it is now admitted that the rule which made mere share in profits the test of liability began in 1793 with the case of Waugh *v.* Carver, and some unsound reasoning of Lord Chief Justice Eyre in that case. It was indeed an excrescence on the body of our laws which was permitted to grow till it had reacted by disease within, but for its removal it was not necessary to rush to the extreme.

And yet I cannot but think its existence had much to do with the public opinion that passed the Limited Liability Act in 1855. Loud was the clamour about the hardship that made capitalists liable as partners if they lent money to a firm, taking their chance of interest according to profits by name, whilst various money lenders, without any such risk, were paid exorbitant interest out of profits in fact. But this anomaly does not logically lead to total exemption from liability of the real controlling proprietors, or those in the apparent

direction, whom the world with right presumes to have interest and heart in its well-being, nor has the limitation of responsibility been yet applied save to joint-stock companies—that is, the publicly registered partnerships of seven or more persons; the members of private partnerships still are liable to their last acre and shilling, and when they are members in fact, and not by implication of law, I see no objection, nor do I believe there is any, in the general opinion that they should remain so. Neither see I reason why the ostensible and active conductors of registered partnerships, on the faith of whose names the public deal, should not be similarly liable.

As the law now stands, a joint-stock company must either remain with liability all unlimited as before 1855, or absolutely limited to the nominal amount of its shares. There is no intermediate. And yet I venture to think not only is there place for one, but that it is by such middle course we shall most safely go to remedy the evils of which we inquire to-night. I do not at present propose to repeal the acts permitting companies with limited liability, but I would by legislation sanction the establishment of registered public companies, whose known directors and whose working shareholders should be liable, like unregistered private partners, to the extent of their means, but whose inactive shareholders, mere contributors of capital, should not be responsible beyond the capital so contributed. I have not time to argue out my reason for believing why a company so formed would carry with it at once the greater advantages which a widely contributed capital ensures to public companies as compared with private firms, and those advantages which a concentrated government is likely to give to private as compared with public enterprizes.

Before approaching the second route I had traced, I would remind you of a large class of cases where, without moral fraud in any one, the shareholding public have been misled into disaster. I mean those cases where, after the publishing of a prospectus not untrue, changes have been made in the scope, objects, or details of the concern, and introduced into the articles of association, whereby the character of the company may be vastly altered. After much discussion it has now been settled that every shareholder must be taken to acquaint himself with the articles of association at the earliest opportunity, and how widely soever the company ultimately formed may differ from that which, from the prospectus, he believed he joined, the shareholder, on the lapse of a reasonable time for registration, is debarred all complaint on this score, and can no longer say, *Non hoc in fœdere veni.* The great number of persons of position and prudence who have been disappointed by this rule creates fresh wonder at the self-abandoning faith of a somewhat Sadducean age.

I next approach the injustices of the present system to shareholders and partners as between themselves. Whatever difference of opinion there are about modifying the principles of limited liability, it is plain some remedy must be applied to the intolerable system of fraud and falsehood which has sprung up under its shelter. For intolerable it is that men are to be drawn into concerns, the very bases of whose constitutions have been studiously concealed from them—concealed for the very intent of indrawing. This

monstrous evil has also grown up in violation of the principles of our common law—using the word in the larger sense to include the doctrines of our courts of equity. By these, the contract of co-partnership, that is, the agreement which binds the members of the firm to each other, is said to be *uberrimæ fidei*—requiring richest good faith. Reason it should be so, for each partner is agent of all the rest, to bind them by his engagements for good and evil. So the trust of each in each must be unqualified, and that cannot exist securely except with perfect mutual candour, and interchange of confidence on those subjects which it is the essential interest of all to know. What ought I to think of the man who as an individual would ask me to become his partner in a ship, he to be the manager and I the dormant owner—concealing from me that his capital in the venture was to consist of the money paid to him by way of bribe by the rascal who had sold him the ship for double its value; the purchase money my contribution, and the bribe taken out of it. And yet this very thing is done every day by gentlemen of standing and character, when they lend their names as purchased directors to the prospectuses of selfish knaves, who pocket what I call swag, and they "promotion-money."

I regret to say that the studious concealment in a company's prospectus of the intended application of its first available capital to purposes which could not have been suspected by any unimitiated, and for which there is neither present equivalent nor future prospect, is not considered illegal in the existing state of our law. In all the cases I have mentioned above, the judges were obliged to throw over this as an element of fraud.

But the most fertile source of deception is the practice of baiting the programmes of an infant company with the names of persons of influence and fortune, nominal directors in every sense, but who have in truth no real interest either of hope or fear in its future life. No language of denunciation can be too strong to stigmatize the laxity by which in apathy or connivance gentlemen of station are found thus to lend their names to the vile use of grasping speculators. This practice, whilst defying palliation, best explains and best reveals the wide-spread gullibility of the modern public. After all, the most prudent investor must take much on trust, and when he reads the rosy-tinted horoscope, and wonders if it be partly true, what can he do but look to the names of the sponsors, and finding these of known honour and integrity, is he then so blameworthy in his simplicity if he assumes that these gentlemen have embarked some fortune and liability in this undertaking, and that their identification with it vouches by the warranty of their word, at least, honesty in its foundation and wise men's faith in its chances? This I know, that high-sounding names are purchased for the purpose of inducing such very faith in the invited shareholder, and for no other cause; and that men whose private lives are of undoubted honour have often sold their names to bubble promoters, to be used as shining flies to kill confiding gudgeons, is one of the melancholy phenomena of our contemporaneous world.

In one of the above mentioned narratives (Henderson's), Lord

Hatherley thus speaks:—"I must say this is one of those cases which surprises one extremely as to the course of proceeding which gentlemen feel themselves justified in taking, and which I am sure if they were individually concerned they would never think of taking in their private affairs." And again, in Ross's case, "Whatever delusions these gentlemen may have been labouring under, and they have been so debauched by the transactions of these companies that they do labour under grievous delusions as to what moral propriety requires, they will not on inspection consider they were justified in so holding out to the public." But as this gregarious conscience is a moral fact, it must be dealt with as a commercial one.

For, as the law now stands, I also regret to say, the announcement of a man's name as a director of a company with his knowledge and assent does not carry with it even the limited liability of fixing him with the minimum of shares which by the company's articles are a director's necessary qualification. Lord Romilly, in the Duke of Abercorn's case, (31 L. J., Ch 828) very clearly and confidently decided that it should and did; but his decision, which seemingly rests on ground unshakable, was reversed upon appeal, and I cannot but think on most questionable reasoning. This is the more regretable, because there was sufficient reason for exempting the Duke in that case on his special equity. His Grace had withdrawn from the Bank of Deposit some years before, but his director's fees were most improperly paid into Coutts's to his account, from time to time, without his knowledge, and to have held him a director or shareholder would have been to give effect to fraud. The startling doctrine that a director may hold no shares at all has more than once been referred to with suspicion, but it is followed ever since as law.

As the law stands, it is not unlawful for a director to hold paid-up shares, that is, shares allocated to him as paid up, and by way of inducement to become a director.

Nor is it unlawful, as the law stands, that a director so induced by paid-up shares should receive out of the promotion money a bonus for his complaisance.

Neither is it unlawful for such a director, as in my last three statements mentioned, to allow his name to go forth in gilded letters on *couleur de rose* prospectus, as chairman, or principal promoter, without any warning or distant hint of his true relation to the company. The above *placita* were established by the cases I have cited above.

Neither is it unlawful for gentlemen to lend their names as provisional directors before incorporation, on a distinct treaty that they are not bound to remain in the company after incorporation. The delusiveness of such a programme needs no enlarging. There was a case tried in Dublin last year, in which a prospectus was proved containing some dozen of well known names of provisional directors. Before the company was registered, every gentleman, save two, had for one reason or other withdrawn from the undertaking, but the shareholders who had read the prospectus never read the letters of resignation—fondly assuming that they joined in joint-stock a fair array of commercial magnates, they little dreamed to find the bril-

liant regiment had elected long since to fold their tents like the Arabs, and as quietly steal away

With cases of fraud, Equity of course professes to deal, but her remedies in the joint-stock cases have been inadequate and uncertain. A man induced to become a shareholder by fraud in statement or suppression has a theoretic right to rescind his contract to take shares, or to bring an action for the deceit. When companies were unlimited, this right usually met the exigency, for the deluded one either got out of his bargain, or he had compensation against a solvent proprietary; but the world knows how in the great Overend-Gurney bubble the deluded shareholders were held fast to their liability, and how the House of Lords affirmed the rule that after a winding-up petition has been filed, no fraud, however diabolical, that made him one can excuse a shareholder from the obligation to contribute, and as the company is now insolvent, he has no hope as against them. It was on this principle Mr. Kent's release by Wood, V.C. was reversed on appeal. The forlorn one may take action at law against the actual fraud perpetrators who had entrapped him, but for success in this he must establish guilty knowlege; then the ringleaders are found to be without means or without the jurisdiction, and against the monied directors proof of the technical *scienter* fails.—See *Western Bank of Scotland* v. *Addie*, (H.L., L.R., 1, sec., ap.)

In like manner it is now settled that, even apart from the winding-up order and rights of creditors thereupon intervening, a shareholder cannot rescind for fraud or misstatement in the prospectus, unless he elects to do so within a reasonable time; and this has been interpreted to be immediately after the means of learning the untruth can be imputed to him. It may easily be supposed, having regard to the scattered and helpless position of ordinary shareholders, how seldom they hunt all available tracks of inquiry, and how often the first knowledge of the deception arrives with the announcement that the company has, in the finical euphemism of the day "gone into liquidation."

I hasten to suggest the changes in the existing rules which I think are called for, and would hope might meet approval with the public and with parliament.

I would make it obligatory that the prospectus and articles of association of every nascent company, whether of limited or unlimited liability, should contain all such information of the circumstances of its promotion as an incoming partner is entitled to have disclosed, according to the rules of law and equity in cases of common-law joint-partnerships. There is nothing revolutionary in this. The analogy of a joint-stock company to a common-law partnership is obvious, and has been constantly applied by the most eminent masters of equity in every branch of companies' law, and in this particular was pointed at by Lord Hatherley in Ross's case thus, "In all these transactions it is essential that there should be *uberrima fides*—a most complete disclosure of the facts, on the part of those who induce the public to invest their money." Notably should it be obligatory, as part of the rule I advocate, that all special circumstances

in connexion with expenses of promotion should be imparted, and that wherever a purchase from a promoter is contemplated, the circumstances of his connexion with the property should be fully made known. Here again the authority of Lord Hatherley supports me. "I *wish* it were the law"—he says in Kent *v.* The Freehold Land Company—"*though I am bound to say it is not*, that everything that is to be given in respect of bonus and promotion money should appear upon the face of the prospectus." A change in this law wished for by such an authority cannot be rash, and must be practicable. The necessity for disclosure would strike at the root of this abominable system of avarice, recklessness, and malversation. Sharks are very formidable when they swim and swallow in the dark of deep waters, but we do not fear them stranded in the day.

So should it be obligatory that intended shareholders should have made known any special circumstances limiting the ostensible liability and interest of their future copartners, whether mere shareholders or directors. Every director should be presumed to hold at least the amount of shares necessary for qualification Common justice and Lord Romilly here support me. Any stipulation to the contrary should be deemed illegal and void, save when the same shall be openly disclosed to the invited shareholders and to the company. Similarly illegal and void, save when similarly disclosed, should be all indemnities against liability as directors, given to persons accepting the office; all bonus, directly or indirectly taken from capital, given them as inducement to take office; and likewise illegal and void should be all issues of paid-up shares to any person, save when the circumstances and consideration of such issue shall have been announced. All this would be but to enforce the right of a partner to know the destination of his own capital, and the conjoint interest of his copartners. Here, too, I think, the necessity for candour would put an end to the twilight-seeking meanness.

Provisional directors, that is, promoting directors named in prospectuses before incorporation, should be bound to the extent of the qualifying amount of shares for a fixed period after incorporation, and at least until the first general meeting of the incorporated shareholders; and then their retirement should be made known. There is too much illusion in a system which permits the apparent architects of those joint-stock houses to disappear from their completed work, like the phantom builders of an Arabian-Night Palace.

I know it is easier to suggest that such rules should be obligatory than to devise a well-working scheme for making them so. After some thought, but not so much as I would have desired to bestow upon this difficulty, I venture thus to treat it:—

To insure that each intended shareholder should be fully informed as to the real nature of the undertaking he is asked to join, I suggest that his contract to take shares should not be complete until one month after the prospectus of the company and its articles of association should have been sent, with the notice of allotment, to his place of abode; these should contain all the information which an incoming partner is entitled to have, and they should be interpreted to speak as of the date of the transmission, so as to com-

pel the imparting of any change which may have occurred since their original publication. It has frequently been decided that notice of allotment is necessary to bind the shareholders' bargain. To compel the transmission of the company's programme entails no additional inconvenience, a month seems not an unreasonable time to allow for consideration, and the *locus penitentiæ;* whilst, unless a positive obligation to disclose all material facts be imposed, it would be easy to evade the consequences of a false programme by publishing none at all, leaving the grossest deception still practicable by moral falsehood, anonymous advertisement, disguised puffs, and purchased editorial praise.

Every fraudulent suppression should carry the consequences of a misdemeanor, as a fraudulent representation already does under Lord Westbury's act of 1857, and that guilt should attach, *primâ facie*, to every one whose name is mentioned on the prospectus or articles as a director or promoter. I do not think this by any means goes too far. It is insufferable that honest men are to give the imprimatur of fair reputations to the reckless lies of conspirators, and shelter themselves from all consequences of the wrongs so wrought by pleading a reckless ignorance of the falsehood to which their fair reputations alone gave currency. If the careless engine-driver who permits my death is guilty of manslaughter, shall the more selfishly careless gentleman who permits my ruin be free from criminal consequence. It is idle to confine the penalty to the actual fabricator, insolvent or *non inventus* at the day of reckoning. Surely it is not too much that every one who thus puts himself before the world as an active originator, should be deemed personally to have made the statements which his name endorses, to have examined their truths or falsehoods, and that he be bound accordingly in every case unless he can prove he has himself been deceived. The good sense of juries would duly check the severity of this rule, and a few commonplace sentences of the world's respectables for commonplace terms of short imprisonment, would do more to stop the evil than isolated penal servitudes once in a generation, when the morbid θαυμα spoils the moral.

But if this be thought to press criminality too far, who can justly object to impose complete civil responsibility in such cases? "If persons," said Lord Cairns in the House of Lords the other day, [*Reese River Mining Co.* v. *Smith*, 4 H. L. 64] "make assertions of facts of which they are ignorant, whether the assertions are true or untrue, they become in a civil point of view as responsible as if they had asserted what they knew to be untrue." Saying so, he expressed a well-known principle of the common law. In Ross's case, Lord Hatherley said: "If directors choose to act upon the representations made by their agent, who was the main promoter and issuer of the prospectus, they must be fixed with the consequences of the transaction, just as if they themselves had borne a part." And in Henderson's case he applied the principle in the way I indicate, to the extent of fixing directors with an imputed *scienter*, a guilty knowledge of misrepresentations in a prospectus concerning their own acts; but in doing so his lordship was forced to admit the doctrine

announced by Lord Cranworth in the Western Bank of Scotland *v.* Addi, [L. R., 1 H. L. sec. 145] that to make directors personally responsible you must fix them with guilty knowledge of the falsehood. His decision, however, and Lord Cairns' aforesaid dictum, fortify that for which I contend—insisting that every statement in a prospectus should be considered the statement of each promoter with the voucher of whose name it goes to the world, and that in an action for deceit its falsehood should be deemed his, save when he could show that he himself was without wilful negligence deceived.

And whether deceived or not, he should be held to warrant all statements so made. Surely he knows his name is used expressly that the world may believe it is he who makes them, and there is no better fixed principle of common law than that every statement made by a contracting party, for the purpose of inducing the contract, is held to be a warranty of its truth which he is bound to make good, however morally innocent or ignorant he may have been.

In closing my task I would freely recognize the difficulties which beset my subject, and if at times I have appeared to use strong words, I would be sorry they were taken to mean dogmatic confidence in the views I offer. They do but indicate for me the feeling of mixed disgust, surprise, and anger, which thickens daily in those large sections of the public who are jealous for the character of our country and the honour of our times, and who, witnessing these recurrent scandals, begin to ask if we are not fallen on degenerate times, in which the successors of the commercial worthies of other days, of the men whose "honour was ennobled into fame," have forfeited their ancient English dower of truth and single purpose. That something must be done is in everybody's confession, and if my reflections be considered partial and my conclusions crude, resting contented with their condemnation, I shall still be rewarded if even in a little I shall have aided to bring higher intelligence than mine to solve what rapidly expands into one of the chief social problems of our day.

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II.—*Some Account of the Laws of the States of New York and Massachusetts regulating the business of Insurance Companies.* By William John Hancock, F.I.A.

[Read Tuesday, the 8th of June, 1869.]

When my learned friend Mr. Falkiner proposed to the Council to read a paper on the very important subject which he has selected, it was stated that arrangements existed in several of the States of the American Union for regulating the business of Insurance Companies. Being officially connected with insurance business in this country, I was requested to prepare a paper with a view to affording the members of this Society some information on the subject. I regret very much that I have been unable to obtain, in time