Revenue Policy Division, who stated that they considered prostitution to be a trade which is fully taxable, and that they, the certified accountants, saw no reason why their client should not be able to organise her business by way of a limited company. They asked whether the name 'Prostitute Ltd' was available for registration as a limited company, pointing out the main object of the company would be that of organising the services of a prostitute.

The registrar did not like that name and did not accept it, nor did he accept another name 'Hookers Ltd' which was offered. But subsequently two further names were offered, 'Lindi St Claire (Personal Services) Ltd' and 'Lindi St Claire (French Lessons) Ltd', and it was the former which he registered.

The memorandum of association said in terms that the first of the objects of the company was 'To carry on the business of prostitution'.

(p. 31) The only director of the company is Lindi St Claire, Miss St Claire describing herself specifically as 'Prostitute'. The other person who owns also one share is a Miss Duggan, who is referred to as 'the cashier'.

Leave having been obtained to apply for judicial review, Miss St Claire wrote in these terms:

> I would like to say that prostitution is not at all unlawful, as you have stated, and I feel it is most unfair of you to take this view, especially when I am paying income tax on my earnings from prostitution to the government Inland Revenue.
>
> Furthermore, I feel it is most unfair of you to imply that I have acted wrongly, as I was most explicit to all concerned about the sole trade of the company to be that of prostitution and nothing more. If my company should not be deemed valid, then it should have not been granted in the first place by the Board of Trade. It is most unfair of the government to allow me to go ahead with my company one moment, then quash it the next. …

It is well settled that a contract which is made upon a sexually immoral consideration or for a sexually immoral purpose is against public policy and is illegal and unenforceable. The fact that it does not involve or may not involve the commission of a criminal offence in no way prevents the contract being illegal, being against public policy and therefore being unenforceable. Here, as the documents clearly indicate, the association is for the purpose of carrying on a trade which involves illegal contracts because the purpose is a sexually immoral purpose and as such against public policy.

Mr Simon Brown submits that if that is the position, as indeed it clearly is on the authorities, then the association of the two or more persons cannot be for 'any lawful purpose'.

To my mind this must follow. It is implicit in the speeches in the Bowman case to which I have just made reference. In my judgment, the contention of the Attorney-General is a valid one and I would order that the registration be therefore quashed.

SKINNER J concurred.

➢ Questions

1. Tom, Dick and Harry wish to incorporate the plumbing business which they have carried on in partnership for some years. What would you say might be (i) the advantages and (ii) the disadvantages for them in buying a ready-made company rather than having one incorporated by their own solicitor?

2. If they do decide to use a ready-made company, what steps will have to be taken in order to transfer the

company to them and to make it fit for their needs?

3. What might be the consequences of the court's order in Miss St Claire's case, in the previous extract, **[1.08]**, so far as concerns acts done in the year that the company was on the register?

Further Reading

BRATTON, W, 'Corporate Law's Race to Nowhere in Particular' (1994) 44 *University of Toronto Law Journal* 401.
Find This Resource

BRATTON, W, 'The Nexus of Contract Corporation: A Critical Appraisal' (1989) 74 *Cornell Law Review* 407.
Find This Resource

DAVIES, PL, *Introduction to Company Law* (2nd edn, 2010), especially ch 1.
Find This Resource

DRURY, R, 'The "Delaware Syndrome": European Fears and Reactions' [2005] JBL 709.
Find This Resource

HANSMANN, H and KRAAKMAN, RH, 'The Essential Role of Organizational Law' (2000) 110 *Yale Law Journal* 387.
Find This Resource

KAHN-FREUD, O, 'Some Reflections on Company Law Reform' (1944) 7 MLR 54.
Find This Resource

(p. 32) KEAY, A, 'Ascertaining the Corporate Objective: An Entity Maximisation and Sustainability Model' (2008) 71 MLR 663.
Find This Resource

KRAAKMAN, RH et al (eds), *The Anatomy of Corporate Law* (2nd edn, 2009), especially ch 1.
Find This Resource

MILMAN, D, 'The Courts and the Companies Acts: The Judicial Contribution to Company Law' [1990] LMCLQ 401.
Find This Resource

STOKES, M, 'Company Law and Legal Theory' in W Twining (ed), *Legal Theory and Common Law* (1986), p 155, and also in S Wheeler (ed), *A Reader on the Law of Business Enterprises* (1994), p 80.
Find This Resource

WEDDERBURN, KW, 'The Social Responsibility of Companies' (1985) 15 *Melbourne University Law Review* 4.
Find This Resource

WOLFF, M, 'On the Nature of Legal Persons' (1938) 54 LQR 494.
Find This Resource

Notes:

[1] Of course, the word 'company' has other meanings in everyday speech; and note in particular the abbreviation 'Co' (and especially '& Co'), which is commonly used as part of the name of an unincorporated partnership that is not a 'company' in any strict legal sense, and is also occasionally used by an individual trader.

[2] A company may also be created by Royal Charter or by special Act of Parliament. Most of these companies are a century or more old. Few such companies still exist, and the rules of 'company law' as derived from the Companies Acts and common law may not always apply to them, eg neither the *ultra vires* doctrine nor the winding-up procedure has traditionally applied to chartered companies (though there are now some exceptions). Beyond this, these types of company are mainly of interest in helping to explain some of the more arcane rules of the subject which evolved long ago and have been allowed to survive into modern times.

[3] CA 2006 ss 58–60. Exceptions are unlimited companies, charitable companies and companies granted a dispensation under ss 60 and 61. There are Welsh equivalents for 'Limited' and 'plc'. The word 'limited' is also used by co-operatives and similar bodies registered under the Industrial and Provident Societies Act 1965, and by limited liability partnerships ('LLP'), under the Limited Liability Partnerships Act 2000.

[4] Companies may also be limited by guarantee. In a company limited by guarantee, the members do not usually pay any money to the company at the outset, but they promise (they 'guarantee') that if the company becomes insolvent, they will pay the amount specified in their guarantee to the company, for the company's use in paying off its creditors. In a company limited by shares, by contrast, the shareholders promise to provide funds to the company by way of the price paid for the share, usually paid in full at the time the share is purchased. That sum is the limit of the shareholder's obligation to contribute to the capital of the company, so if the company becomes insolvent, all the shareholder is required to pay to support the company is the amount (if any) still unpaid on the shares. See Insolvency Act 1986 (IA 1986) s 74.

[5] Unless the company is an unlimited company (see 'Limited and unlimited companies: CA 2006 s 3', p 20).

[6] Some risky corporate ventures (eg historically, mining ventures) are set up this way to persuade outside funders of the confidence of the members in the likely success of the planned venture. But it is more usual now, in these types of cases, to set up a company limited by shares and require the shareholders (and directors) to provide unlimited personal guarantees of the company's debts. The two structures are functionally equivalent.

[7] See fn 4.

[8] For further reading, see PL Davies, *Introduction to Company Law* (2nd edn, 2010); and RH Kraakman et al (eds), *The Anatomy of Corporate Law* (2nd edn, 2009).

[9] The full implementation timetable is available on the BIS website: www.bis.gov.uk/files/file53065.pdf. For a list of Regulations and Commencement Orders see:http://webarchive.nationalarchives.gov.uk/20121029131934/ http:/www.bis.gov.uk/policies/business-law/company-and-partnership-law/company-law/regulations-statutory-instruments.

[10] Especially the IA 1986 and the Financial Services and Markets Act 2000 (FSMA 2000), and the company-specific Company Directors Disqualification Act 1986, but also by statutes that apply generally to 'legal persons', such as the Sale of Goods Act 1979 and various Property Law Acts.

[11] Law Commission, *Company Directors: Regulating Conflicts of Interests and Formulating a Statement of Duties* (Law Com No 261, 1999) (available at:http://lawcommission.justice.gov.uk/docs/lc261_Company_Directors.pdf). This was preceded by a Consultation Paper (LCCP 153, September 1998) which is available at:http://lawcommission.justice.gov.uk/docs/cp153_Company_Directors_Consulation.pdf and which usefully sets out the Commission's understanding of the current law. Also Law Commission, *Shareholder Remedies* (Law Com No 246, 1997) available at: http://lawcommission.justice.gov.uk/docs/lc246_Shareholder_Remedies.pdf, and the preceding Consultation Paper (LCCP 142, 1996), available at: http://lawcommission.justice.gov.uk/docs/cp142_Shareholder_Remedies_Consultation.pdf.

[12] All of these documents may be downloaded from the BIS website: www.gov.uk/company-and-partnership-law--2 (click on Contents: Company Law review).

[13] www.bis.gov.uk/assets/biscore/business-law/docs/e/10-1362-evaluation-companies-act-2006-executive-summary.pdf.

[14] The Companies Clauses Consolidation Act 1845, which is still in force, applies to these 'statutory' companies. This Act contains standard provisions which may be incorporated by reference into the particular Act, so making the procedure shorter and cheaper.

[15] Eg on company investigations, see Chapter 14.

[16] Since repealed and replaced by the Criminal Justice Act 1993 Pt V.

[17] The DTI's Review (Modern Company Law for a Competitive Economy): published Consultation Documents: No 1 (February 1999): *The Strategic Framework* (URN 99/654)

No 2 (October 1999): *Company General Meetings and Shareholder Communication* (URN 99/1144) No 3 (October 1999): *Company Formation and Capital Maintenance* (URN 99/1145)

No 4 (October 1999): *Reforming the Law Concerning Overseas Companies* (URN 99/1146)

No 5 (March 2000): *Developing the Framework* (URN 00/656)

No 6 (June 2000): *Capital Maintenance—Other Issues* (URN 00/880)

No 7 (October 2000): *Registration of Company Charges* (URN 00/1213)

No 8 (November 2000): *Completing the Structure* (URN 00/1335). See fn 12.

[18] See the European Commission's Internal Market website: http://ec.europa.eu/internal_market/index_en.htm.

[19] A range of SIs continue the technical implementation of Regulations and Directives. The full list is available at www.berr.gov.uk/policies/business-law/company-and-partnership-law/company-law/regulations-statutory-instruments and the Explanatory Memorandum details the European history of each.

[20] [1986] ECR 723, [1986] 1 CMLR 688.

[21] [1984] ECR 1891, [1986] 2 CMLR 430 at para [26].

[22] Supplemented by the EEIG Regulations (SI 1989/638), which set out in Sch 1 the full text of the EU Regulation.

[23] For a recent report published as part of a review process on the functioning of the SEs by the European Commission: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0676:FIN:EN:PDF.

[24] See 'Inspections and subsequent fair trials—criminal and civil cases', p 737.

[25] These reports include: Loreburn Committee, reported 1906, leading to Companies Acts of 1907–08; Wrenbury Committee, reported 1918; Greene Committee, reported 1926, leading to Companies Acts of 1928–29; Bodkin Committee, reported 1937 (sharepushing), leading to Prevention of Fraud (Investments) Act 1939; Anderson Committee, reported 1936 (unit trusts); Cohen Committee, reported 1945, leading to Companies Acts of 1947–48; Gedge Committee, reported 1954 (no par value shares); Jenkins Committee, reported 1962; Bullock Committee, reported 1977 (employee representation); Wilson Committee, reported 1980 (financial institutions); Cork Committee, reported 1982 (insolvency), leading to Insolvency Acts of 1985 and 1986; Gower, *Review of Investor Protection*, reported 1984, leading to Financial Services Act 1986; Prentice, *Reform of the Ultra Vires Rule*, reported 1986, leading to reforms in CA 1989; Dearing, *The Making of Accounting Standards*, reported 1988; Diamond, *A Review of Security Interests in Property*, reported 1989 (company charges).

[26] See especially the consultations on directors' duties and the remedies available to minority shareholders.

[27] 'Core' company law was taken to include the essential principles of company law that are common to all companies, or at least to large categories of companies such as public companies or private companies. The intention was that new legislation would exclude provisions that only applied to companies that fell into a special class for reasons unrelated to company law (eg charitable companies), or that were better treated in other

statutes, eg the rules governing the offering of shares to the public, which are now dealt with as part of the securities regulation.

[28] See http://webarchive.nationalarchives.gov.uk/+/ http://www.bis.gov.uk/policies/business-law/company-and-partnership-law/evaluation%20of%20companies%20act%202006.

[29] The CLR terms this topic the 'scope' issue, putting the question: 'For what purpose and in whose interests should companies be operated and controlled?' It is more commonly referred to as the 'stakeholder' debate, and in this book is discussed under the heading of directors' duties, at Chapter 7.

[30] There is as yet no detail on the proposal: /www.gov.uk/company-and-partnership-law--2.

[31] This was in Scotland. In England, the lender would typically have taken a charge, and so there would have been no transfer of legal ownership of the shares. See Chapter12.

[32] See current proposals for the application of CA 2006 to Limited Liability Partnerships (The Draft Limited Liability Partnerships (Application of Companies Act 2006) Regulations 2009). See also D Sutherland, 'Limited Liability Partnerships: All Change with the Companies Act 2006?' (2008) 7 JIBFL 340.

[33] Incorporation documents may be filed electronically.

[34] This is only compulsory for public companies: CA 2006 s 12.

[35] And can therefore only be questioned by the AG, because the Act does not bind the Crown (per Lord Parker of Waddington in *Bowman v Secular Society Ltd* **[1.06]** at 438–440, and *Cotman v Brougham* [1918] AC 514 at 519). For an example of a request for reversal of a decision to register a company, see *R v Registrar of Companies, ex p AG* **[1.08]**.

[36] [1896] 2 Ch 679.

[37] The use of the term 'quasi-judicial' is misleading. This function of the registrar can only be described as 'ministerial': as we have seen earlier, in the matter of registration, he exercises no discretionary powers, still less is he concerned to adjudicate any dispute.

[38] See R Drury, 'Nullity of Companies in English Law?' (1985) 48 MLR 625.

2. Corporate Personality and Limited Liability

Chapter: **(p. 33)** 2. Corporate Personality and Limited Liability
Author(s): Len Sealy and Sarah Worthington
DOI: 10.1093/he/9780199676446.003.0002

General issues

We saw in the previous chapter that the separate legal personality of a company and the limited liability of its members are two key consequences of incorporation of limited companies. Both of these ideas are examined in more detail here.[1]

First, consider the idea of a company's separate legal personality, or the idea that it is a legal person in its own right, separate from the legal persons that are its members (or shareholders) and its directors. In ordinary speech, we use the word 'person' to refer to an individual human being. But in law the word has a more technical meaning: 'a subject of rights and duties'.[2] In this sense it is possible to speak of a corporation as a 'person' and recognise its separate 'personality'.

(p. 34) ***A company is a legal person separate and distinct from its members.***

[2.01] Salomon v A Salomon & Co Ltd [1897] AC 22 (House of Lords)[3]

The facts and arguments appear from the speech of Lord Macnaghten. Some extracts from the judgments of the trial judge and the Court of Appeal are given at **[2.02]**.

> LORD MACNAGHTEN: Mr Salomon, who is now suing as a pauper, was a wealthy man in July 1892. He was a boot and shoe manufacturer trading on his own sole account under the firm of 'A Salomon & Co', in High Street, Whitechapel, where he had extensive warehouses and a large establishment. He had been in the trade over thirty years. He had lived in the same neighbourhood all along, and for many years past he had occupied the same premises. So far things had gone very well with him. Beginning with little or no capital, he had gradually built up a thriving business, and he was undoubtedly in good credit and repute.
>
> It is impossible to say exactly what the value of the business was. But there was a substantial surplus of assets over liabilities. And it seems to me to be pretty clear that if Mr Salomon had been minded to dispose of his business in the market as a going concern he might fairly have counted upon retiring with at least £10,000 in his pocket.
>
> Mr Salomon, however, did not want to part with the business. He had a wife and a family consisting of five sons and a daughter. Four of the sons were working with their father … But the sons were not partners: they were only servants. Not unnaturally, perhaps, they were dissatisfied with their position. They kept pressing their father to give them a share in the concern. 'They troubled me,' says Mr Salomon, 'all the while.' So at length Mr Salomon did what hundreds of others have done under similar circumstances. He turned his business into a limited company. He wanted, he says, to extend the business and make provision for his family. In those words, I think, he fairly describes the principal motives which influenced his action.
>
> All the usual formalities were gone through; all the requirements of the Companies Act 1862 were duly observed. There was a contract with a trustee in the usual form for the sale of the business to a company about to be formed. There was a memorandum of association duly signed and registered, stating that the company was formed to carry that contract into effect, and fixing the capital of £40,000 in 40,000 shares of £1 each. There were articles of association providing the usual machinery for conducting the business. The first directors were to be nominated by the majority of the subscribers to the memorandum of association.

The directors, when appointed, were authorised to exercise all such powers of the company as were not by statute or by the articles required to be exercised in general meeting; and there was express power to borrow on debentures, with the limitation that the borrowing was not to exceed £10,000 without the sanction of a general meeting.

The company was intended from the first to be a private company;[4] it remained a private company to the end. No prospectus was issued; no invitation to take shares was ever addressed to the public.

The subscribers to the memorandum were Mr Salomon, his wife, and five of his children who were grown up. The subscribers met and appointed Mr Salomon and his two elder sons directors. The directors then proceeded to carry out the proposed transfer. By an agreement dated 2 August 1892 the company adopted the preliminary contract, and in accordance with it the business was taken over by the company as from 1 June 1892. The price fixed by the contract was duly paid. **(p. 35)** The price on paper was extravagant. It amounted to over £39,000—a sum which represented the sanguine expectations of a fond owner rather than anything that can be called a businesslike or reasonable estimate of value. That, no doubt, is a circumstance which at first sight calls for observation; but when the facts of the case and the position of the parties are considered, it is difficult to see what bearing it has on the question before your Lordships. The purchase-money was paid in this way: as money came in, sums amounting in all to [£20,000][5] were paid to Mr Salomon, and then immediately returned to the company in exchange for fully paid shares. The sum of £10,000 was paid in debentures[6] for the like amount. The balance, with the exception of about £1,000 which Mr Salomon seems to have received and retained, went in discharge of the debts and liabilities of the business at the time of the transfer, which were thus entirely wiped off. In the result, therefore, Mr Salomon received for his business about £1,000 in cash, £10,000 in debentures, and half the nominal capital of the company in fully paid shares for what they were worth. No other shares were issued except the seven shares taken by the subscribers to the memorandum, who, of course, knew all the circumstances, and had therefore no ground for complaint on the score of overvaluation.

The company had a brief career: it fell upon evil days. Shortly after it started there seems to have come a period of great depression in the boot and shoe trade. There were strikes of workmen too; and in view of that danger contracts with public bodies, which were the principal source of Mr Salomon's profit, were split up and divided between different firms. The attempts made to push the business on behalf of the new company crammed its warehouses with unsaleable stock. Mr Salomon seems to have done what he could: both he and his wife lent the company money; and then he got his debentures cancelled and reissued to a Mr Broderip, who advanced him £5,000, which he immediately handed over to the company on loan. The temporary relief only hastened ruin. Mr Broderip's interest was not paid when it became due. He took proceedings at once and got a receiver appointed. Then, of course, came liquidation and a forced sale of the company's assets. They realised enough to pay Mr Broderip, but not enough to pay the debentures in full: and the unsecured creditors were consequently left out in the cold.

In this state of things the liquidator met Mr Broderip's claim by a counter-claim, to which he made Mr Salomon a defendant. He disputed the validity of the debentures on the ground of fraud. On the same ground he claimed rescission of the agreement for the transfer of the business, cancellation of the debentures, and repayment by Mr Salomon of the balance of the purchase-money. In the alternative, he claimed payment of £20,000 on Mr Salomon's shares, alleging that nothing had been paid on them.

When the trial came on before Vaughan Williams J,[7] the validity of Mr Broderip's claim was admitted, and it was not disputed that the 20,000 shares were fully paid up. The case presented by the liquidator broke down completely; but the learned judge suggested that the company had a right of indemnity against Mr Salomon. The signatories of the memorandum of association were, he said, mere nominees of Mr Salomon —mere dummies. The company was Mr Salomon in another form. He used the name of the company as an alias. He employed the company as his agent; so the company, he thought, was entitled to indemnity against its principal. The counter-claim was accordingly amended to raise this point; and on the amendment being made the learned judge pronounced an order in accordance with the view he had expressed.

The order of the learned judge appears to me to be founded on a misconception of the scope and effect of

the Companies Act 1862. In order to form a company limited by shares, the Act requires that a memorandum of association should be signed by seven persons, who are each to take one **(p. 36)** share at least. If those conditions are complied with, what can it matter whether the signatories are relations or strangers? There is nothing in the Act requiring that the subscribers to the memorandum should be independent or unconnected, or that they or any one of them should take a substantial interest in the undertaking, or that they should have a mind and will of their own, as one of the learned Lords Justices seems to think, or that there should be anything like a balance of power in the constitution of the company. In almost every company that is formed the statutory number is eked out by clerks or friends, who sign their names at the request of the promoter or promoters without intending to take any further part or interest in the matter.

When the memorandum is duly signed and registered, though there be only seven shares taken, the subscribers are a body corporate 'capable forthwith', to use the words of the enactment, 'of exercising all the functions of an incorporated company'. Those are strong words. The company attains maturity on its birth. There is no period of minority—no interval of incapacity. I cannot understand how a body corporate thus made 'capable' by statute can lose its individuality by issuing the bulk of its capital to one person, whether he be a subscriber to the memorandum or not. The company is at law a different person altogether from the subscribers to the memorandum; and, though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustee for them. Nor are the subscribers as members liable, in any shape or form, except to the extent and in the manner provided by the Act. That is, I think, the declared intention of the enactment. If the view of the learned judge were sound, it would follow that no common law partnership could register as a company limited by shares without remaining subject to unlimited liability.

Mr Salomon appealed; but his appeal was dismissed with costs, though the appellate court did not entirely accept the view of the court below.[[8]] …

Among the principal reasons which induce persons to form private companies, as stated very clearly by Mr Palmer in his treatise on the subject, are the desire to avoid the risk of bankruptcy, and the increased facility afforded for borrowing money. By means of a private company, as Mr Palmer observes, a trade can be carried on with limited liability, and without exposing the persons interested in it in the event of failure to the harsh provisions of the bankruptcy law. A company, too, can raise money on debentures, which an ordinary trader cannot do. Any member of a company, acting in good faith, is as much entitled to take and hold the company's debentures as any outside creditor. Every creditor is entitled to get and to hold the best security the law allows him to take.

If, however, the declaration of the Court of Appeal means that Mr Salomon acted fraudulently or dishonestly, I must say I can find nothing in the evidence to support such an imputation. The purpose for which Mr Salomon and the other subscribers to the memorandum were associated was 'lawful'. The fact that Mr Salomon raised £5,000 for the company on debentures that belonged to him seems to me strong evidence of his good faith and of his confidence in the company. The unsecured creditors of A Salomon and Co Ltd may be entitled to sympathy, but they have only themselves to blame for their misfortunes. They trusted the company, I suppose, because they had long dealt with Mr Salomon, and he had always paid his way; but they had full notice that they were no longer dealing with an individual …

It has become the fashion to call companies of this class 'one man companies'. That is a taking nickname, but it does not help one much in the way of argument. If it is intended to convey the meaning that a company which is under the absolute control of one person is not a company legally incorporated, although the requirements of the Act of 1862 may have been complied with, it is inaccurate and misleading: if it merely means that there is a predominant partner possessing an overwhelming influence and entitled practically to the whole of the profits, there is nothing in that that I can see contrary to the true intention of the Act of 1862, or against public policy, or detrimental **(p. 37)** to the interests of creditors. If the shares are fully paid up, it cannot matter whether they are in the hands of one or many. If the shares are not fully paid, it is as easy to gauge the solvency of an individual as to estimate the financial ability of a crowd.

One argument was addressed to your Lordships which ought perhaps to be noticed, although it was not the ground of decision in either of the courts below. It was argued that the agreement for the transfer of the business to the company ought to be set aside, because there was no independent board of directors, and the property was transferred at an overvalue. There are, it seems to me, two answers to that argument. In the first place, the directors did just what they were authorised to do by the memorandum of association. There was no fraud or misrepresentation, and there was nobody deceived. In the second place, the company have put it out of their power to restore the property which was transferred to them …

LORD HALSBURY LC: My Lords, the important question in this case, I am not certain it is not the only question, is whether the respondent company was a company at all—whether in truth that artificial creation of the legislature had been validly constituted in this instance; and in order to determine that question it is necessary to look at what the statute itself has determined in that respect. I have no right to add to the requirements of the statute, or to take from the requirements thus enacted. The sole guide must be the statute itself.

Now, that there were seven actual living persons who held shares in the company has not been doubted. As to the proportionate amounts held by each I will deal presently; but it is important to observe that this first condition of the statute is satisfied, and it follows as a consequence that it would not be competent to any one—and certainly not to these persons themselves—to deny that they were shareholders.

I must pause here to point out that the statute enacts nothing as to the extent or degree of interest which may be held by each of the seven, or as to the proportion of interest or influence possessed by one or the majority of the shareholders over the others. One share is enough. Still less is it possible to contend that the motive of becoming shareholders or of making them shareholders is a field of inquiry which the statute itself recognises as legitimate. If they are shareholders, they are shareholders for all purposes; and even if the statute was silent as to the recognition of trusts, I should be prepared to hold that if six of them were [trustees for] the seventh, whatever might be their rights inter se, the statute would have made them shareholders to all intents and purposes with their respective rights and liabilities, and, dealing with them in their relation to the company, the only relations which I believe the law would sanction would be that they were corporators of the corporate body.

I am simply here dealing with the provisions of the statute, and it seems to me to be essential to the artificial creation that the law should recognise only that artificial existence—quite apart from the motives or conduct of individual corporators. In saying this, I do not at all mean to suggest that if it could be established that this provision of the statute to which I am adverting had not been complied with, you could not go behind the certificate of incorporation to show that a fraud had been committed upon the officer entrusted with the duty of giving the certificate, and that by some proceeding in the nature of scire facias you could not prove the fact that the company had no real legal existence. But short of such proof it seems to me impossible to dispute that once the company is legally incorporated it must be treated like any other independent person with its rights and liabilities appropriate to itself, and that the motives of those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are.

I will for the sake of argument assume the proposition that the Court of Appeal lays down—that the formation of the company was a mere scheme to enable Aron Salomon to carry on business in the name of the company. I am wholly unable to follow the proposition that this was contrary to the true intent and meaning of the Companies Act. I can only find the true intent and meaning of the Act from the Act itself; and the Act appears to me to give a company a legal existence with, as I have said, rights and liabilities of its own, whatever may have been the ideas or schemes of those who brought it into existence.

(p. 38) I observe that the learned judge (Vaughan Williams J) held that the business was Mr Salomon's business, and no one else's, and that he chose to employ as agent a limited company; and he proceeded to argue that he was employing that limited company as agent, and that he was bound to indemnify that agent (the company). I confess it seems to me that that very learned judge becomes involved by this argument in a very singular contradiction. Either the limited company was a legal entity or it was not. If it was, the business belonged to it and not to Mr Salomon. If it was not, there was no person and no thing to

be an agent at all; and it is impossible to say at the same time that there is a company and there is not.

Lindley LJ, on the other hand, affirms that there were seven members of the company; but he says it is manifest that six of them were members simply in order to enable the seventh himself to carry on business with limited liability. The object of the whole arrangement is to do the very thing which the legislature intended not to be done.[9]

It is obvious to inquire where that intention of the legislature manifested in the statute is. Even if we were at liberty to insert words to manifest that intention, I should have great difficulty in ascertaining what the exact intention thus imputed to the legislature is, or was. In this particular case it is the members of one family that represent all the shares; but if the supposed intention is not limited to so narrow a proposition as this, that the seven shareholders must not be members of one family, to what extent may influence or authority or intentional purchase of a majority among the shareholders be carried so as to bring it within the supposed prohibition? It is, of course, easy to say that it was contrary to the intention of the legislature—a proposition which, by reason of its generality, it is difficult to bring to the test; but when one seeks to put as an affirmative proposition what the thing is which the legislature has prohibited, there is, as it appears to me, an insuperable difficulty in the way of those who seek to insert by construction such a prohibition into the statute.

As one mode of testing the proposition, it would be pertinent to ask whether two or three, or indeed all seven, may constitute the whole of the shareholders? Whether they must be all independent of each other in the sense of each having an independent beneficial interest? And this is a question that cannot be answered by the reply that it is a matter of degree. If the legislature intended to prohibit something, you ought to know what that something is. All it has said is that one share is sufficient to constitute a shareholder, though the shares may be 100,000 in number. Where am I to get from the statute itself a limitation of that provision that that shareholder must be an independent and beneficially interested person? …

My Lords, the learned judges appear to me not to have been absolutely certain in their own minds whether to treat the company as a real thing or not. If it was a real thing; if it had a legal existence, and if consequently the law attributed to it certain rights and liabilities in its constitution as a company, it appears to me to follow as a consequence that it is impossible to deny the validity of the transactions into which it has entered. …

LORDS WATSON and DAVEY delivered concurring opinions. LORD MORRIS concurred.

➢ Questions

1. To what do you think Lord Macnaghten was alluding when he said that the unsecured creditors of the company 'had full notice that they were no longer dealing with an individual'? Was it fair to say that 'they have only themselves to blame for their misfortunes'?

2. *Salomon*'s case has been described as a 'calamitous decision' (O Kahn-Freund (1944) 7 MLR 54). Would you agree?

(p. 39) 3. Was there a 'very singular contradiction' in the reasoning of Vaughan Williams J, as Lord Halsbury said? (Compare *Re FG Films Ltd* **[2.14]**, in which the company *was* held to be carrying on business as the agent of its principal shareholder.)

➢ Note

It makes no difference to the rule in *Salomon* that one member owns all or substantially all of the shares. Until 1992, when the Twelfth EU Directive on Single-Member Companies was implemented in the UK, it was necessary for a company to have at least two members. (The number in 1844 was originally set at 25, but this number was reduced to seven by the Companies Act 1862—the Act under which Mr Salomon's company was registered—and later to two.) However, even under the former law it was possible for one person to own all the shares in a company *beneficially* and at the same time comply with the legislation by the simple expedient of vesting one or more shares in nominees who held the shares on his behalf and acted at his direction. In many other jurisdictions, the one person company has been recognised for a long time.

The judgments in the lower courts in *Salomon*'s case (reported as *Broderip v Salomon* **[2.02]**) deserve study in their own right as examples of 'piercing or lifting the veil'. (For this topic, see 'Limited liability of members and "Lifting the corporate veil"', p 51.)

[2.02] Broderip v Salomon [1895] 2 Ch 323 (Chancery Division and Court of Appeal)

> VAUGHAN WILLIAMS J: No charge of fraud … is involved in the amended claim; but to allow a man who carries on business under another name to set up a debenture in priority to the claims of the creditors of the company would have the effect of defeating and delaying his creditors. There must be an implied agreement by him to indemnify the company. Under the Companies Act of 1862 a man may become what is called a private company so as to obtain the benefits of limited liability. I have already held, in a case where the founder of such a company had become bankrupt and the company claimed his assets, that the company was a mere fraud, and the Court of Appeal supported that decision. In this case I propose to hold the same thing—that this business was Mr Salomon's business and no one else's; that he chose to employ as agent a limited company; that he is bound to indemnify that agent, the company; and that his agent, the company, has a lien on the assets which overrides his claims. The creditors of the company could, in my opinion, have sued Mr Salomon. Their right to do so would depend on the circumstances of the case, whether the company was a mere alias of the founder or not. In this case it is clear that the relationship of principal and agent existed between Mr Salomon and the company …
>
> [His Lordship accordingly ordered that Salomon was bound to indemnify the company for the debts which, as his agent, it had incurred.
>
> Salomon appealed to the Court of Appeal, which affirmed this decision on different grounds:] LINDLEY LJ: The incorporation of the company cannot be disputed. (See s 18 of the Companies Act 1862 [Companies Act 2006 (CA 2006), ss 15 and 16].) Whether by any proceedings in the nature of a scire facias the court could set aside the certificate of incorporation is a question which has never been considered, and on which I express no opinion;[10] but, be that as it may, in such an action as this the validity of the certificate cannot be impeached. The company must, therefore, be regarded as a corporation, but as a corporation created for an illegitimate purpose. Moreover, there having always been seven members, although six of them hold only one £1 share each, **(p. 40)** Mr Aron Salomon cannot be reached under s 48 [CA 2006, ss 437 and 438] to which I have already alluded. As the company must be recognised as a corporation, I feel a difficulty in saying that the company did not carry on business as a principal, and that the debts and liabilities contracted in its name are not enforceable against it in its corporate capacity. But it does not follow that the order made by Vaughan Williams J is wrong. A person may carry on business as a principal and incur debts and liabilities as such, and yet be entitled to be indemnified against those debts and liabilities by the person for whose benefit he carries on the business. The company in this case has been regarded by Vaughan Williams J as the agent of Aron Salomon. I should rather liken the company to a trustee for him—a trustee improperly brought into existence by him to enable him to do what the statute prohibits. It is manifest that the other members of the company have practically no interest in it, and their names have merely been used by Mr Aron Salomon to enable him to form a company, and to use its name in order to screen himself from liability … In a strict legal sense the business may have to be regarded as the business of the company; but if any jury were asked, Whose business was it? they would say Aron Salomon's, and they would be right, if they meant that the beneficial interest in the business was his. I do not go so far as to say that the creditors of the company could sue him. In my opinion, they can only reach him through the company. Moreover, Mr Aron Salomon's liability to indemnify the company in this case is,