

Rationale and Impact of Salmon v Salmon (1897) acc 22 on English Company Law 1

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Introduction

The case of Salomon v Salomon and company (1897) acc 22 was a major decision and rule that affects judicial processes to date. A lot of jurisprudence was set from this case that had considerable magnanimity. The decision reached has from the year of the case, 1897, necessitated overwhelming consequences that define the tenets of company law. In addition, it has been of great reference in corporate disputes that arise world over. It is a rule that has elicited praise and criticism in equal measure. It however cemented the doctrine of corporate personality as is established in the Companies act of 1862. This decision was reached to protect the company shareholders from being sued by creditors to pay up unresolved arrears in case the company became bankrupt. This paper examines the issues in Salmon v Salmon (1897), how the court ruled, factors that dictated this ruling and the impact that the ruling has had on the judicial process.

The facts of the case

Mr. Salomon Aron ran a successful business that manufactured leather boots and shoes. Once his sons came of age, they developed a particular interest for joining their father to run the business. In fact, they wanted to be partners of their father in the same business. Mr. Salomon therefore made a decision to convert his business into a limited entity. The business was bought from Mr. Salomon by the new company at 39, 000 pounds. This amount however superseded the real value of the business. In addition, Mr. Salomon included his spouse and five other children as enterprise subscribers. He nominated two of his sons as the company's directors. With this

kind of arrangement, it essentially meant that the company was in reality Mr. Salomon's. Out of the company's total shares of 20,007, Salomon owned and controlled 20,001 shares.

On the 1st of June 1892, the company was legally and officially incorporated. Furthermore, the company dished out debentures worth 10000 pounds to Salomon. This is a form of liability that has no collateral or physical resources as security. Its only security is the solvency and standing of the issuer. As part of the safety to his debentures, Salomon acknowledged 5000 pounds from Edmund Broderip. However, just after the business was integrated, the enterprise began to go down as the sale of boots deteriorated astronomically. The problems were worsened by the constant strike of workers. The major market for Salomon was the government and so in a bid to sidestep the danger of its providers being crippled by the forays, the government went ahead and fragmented the contracts (Armour, 2003).

Eventually, the business was botched. He shirked on interest returns on the debentures, half of which were held by Broderip. Consequently, in October 1893, Broderip went to court demanding to be paid his 5000 pounds which was a security. The company was driven into insolvency and so Broderip subsequently recovered his security. This move left the company with 1055 pounds worth of assets. This remainder was requested by Salomon as payment for the loan he gave the company. With this move, it was obvious that unsafe creditors would be left penniless yet the company owed them a total of 7,773 pounds. After the business botched, a decision made by the receiver stopped the veneration of the floating trust. It was decided that Salmon be made to settle the company's financial burden. It did not go down well with him and he sought the intervention of the court.

Disputes

Acting for the company, the liquidator opposed Salmon's claims in court and demanded that the money paid to him be returned. It even proposed that Salmon's debentures be annulled. It was reasoned that Salmon had intentionally gone against his onus in vending his enterprise for a disproportionate financial value. Fraud against the unsafe creditors was another charge labelled against him.

The resolution of the High Court

The case was presided over by Vaughan Williams J who ruled in favor of Mr. Broderip. The judge held the assertion as legal and positive. The payment of the 200 shares was found to have been remitted and hence there was no disagreement. It was ruled that coverage against Salmon was actually a right possessed by the collapsed company. He ruled that other shareholders that included the daughter, wife and sons were not realistic and that the real owner of the company was Mr. Aron Salmon. Therefore, in case of collapse, the company was supposed to be covered by Salmon himself. The judge ruled that the incorporated company was actually an identity of Salmon who according to the judge was its agent in his business. Finally, an indemnity honor was reached by the High Court.

The decision of the Appeal Court

Salmon appealed the judgment of the high court. However, the court of appeal reasserted the decision earlier reached by the High Court. What informed this decision nonetheless was different. It was a slight departure from the previous ruling. It affirmed that Salmon had ill-treated the freedoms of incorporation and restricted liability. This restricted liability and the law governing incorporation had been set by the legislature to strictly be applied to completely autonomous and legally recognized shareholders who possessed the power and self-will and not

entities who could easily be manipulated (Cheffins, 1997). In concluding that the company was like a trustee to Mr. Salmon, he was thus obligated by law to cover all the debts accrued by the company while it was operating.

The fact that the company was incorporated was neither in doubt nor dispute as it was constituted by the statutes under the companies Act 1862. The judge however declined to give an opinion touching on the company's certificate. The only malice was the resolve for which the company was created. That resolve was considered unlawful. This was so because of the six shareholders among the total seven, possessed just a share each. Therefore the debts owed by the company could not be prescribed against it in its position as a corporation. The judge ruled that the company was a trustee of Salmon which he took advantage of to help him achieve what is illegal as per the statutes. The other shareholders were not in any way important in the daily running of the business and were thus used to shield Mr. Salmon from any eventual liability.

The judge also ruled that the creditors had no legal basis for taking him to court and that they could only settle their issues when they address their grievances to the company and not Salmon as an individual. The result of forming the company to pursue self-interests was actually ascribed to settling the accrued arrears. The compensation does not arise just because he held an extreme majority of the shares as a person can do the same and not be ordered to offer similar compensation. Salmon's illegality is found in the objectives and intentions for which he shaped the company, on the design of its creation and the benefits for which he got as a result of all these illegal maneuvers.

Additionally, the burden of inspecting the register of the company by persons dealing with it was found unfair according to s.43 of the company statute. This can only happen when the creditors are suspicious that may be the other side of the bargain may not be honored.

Otherwise, without those suspicions, creditors possess no freedom to inspect the register of the company (Davies, 2008). Had they inspected the company register, there is a possibility they could have noticed something sinister in the design of shareholding. Mr. Salmon and his associates were cognizant of this fact. As a matter of principle, if it were that the burden of shouldering liability could by extension include the creditors, then it is apparent that parliament while making the act could have instituted appropriate legal cushioning. In light of this fact, the actions of Mr. Aron Salmon were deemed as a swindle. The incorporation of the business was thus a fraudulent plot intended to enable Salmon run his enterprise as usual but with restricted liability.

The ruling of the House of Lords.

The House of Lords, in complete unison, reversed the decisions previously reached by the Court of Appeal. By taking the ruling of the High Court to be based on Salmon being seen as an agent of the company and the Court of Appeal referring to Salmon a fraudster, these positions were overruled (Horwitz, 2001). The House of Lords intimated that in the company act of 1862, there was no mention that the shareholders of the company must independent of the mainstream shareholder. This meant that there was absolutely nothing wrong or a miss in Salmon decision to incorporate the business using his spouse and off springs. It ruled that the company's constitution was legal and that the previous judge's decision was not backed by law but by their own limitations.

Lord Halsbury LC stated that the law did not in any way describe the range that might be controlled by the seven shareholders or the level of influence attributed to one or the highest over the other persons. Lord Halsbury argued that even he held no power to augment the rations of the statute or subtract and that his sole direction was dictated entirely by the law itself. He held that

if indeed the incorporated business was legal, then the ownership of the company was upon the company and not Mr. Salmon. If it was on the other hand illegal, then being agent or a trustee rises not because there is nothing for which one can be agent (Davies, 2010). The company is thus nonexistent. Lord Herschell argued that the claim that all the seven members of the company held no influence was inadequate as there were companies that had more than seven shareholders who were in essence impartial and held no control whatsoever in the running of that particular company.

Lord Macpherson held that there was no breach of law in Salmon assuming advantage of the legalities enshrined in the act as he was allowed to by law. The lord said it was not within the power of the Judges to put their own interpretations of the law based on their personal views. In his own ruling he saw no crimes on Salmon's part. This is one of the aspects of the ruling that led to overturning of the decision made by the court of appeal. (Davies, 2001)

Impact of the ruling

This case had tremendous judicial and legislative effects on the citizens. So many cases since this case have been decided while using this case as a concrete jurisprudence. It led to enforcing the doctrine where a personal of legal standing is considered so much distinct and independent from that of other individual entities. This state of legal personality is protected by the statutes and it continues to bind until such a time when the legal corporate partnership is halted lawfully. This enshrined the doctrine of a separate corporate personality.

This judicial separation comes into effect as soon as the corporation is registered as one of legal twists of the process. This is a standing that still exists even in the commercial partnerships act. There are so many notable merits that comes up with this concept of company

corporate personality (outlaw.com, 2010). The company as a legal entity completely separate from its members in terms of the directors, shareholders and creditors, can actually within the law own its own assets, possess its singular independent freedoms and limitations and is also entitled to its own documented obligations. This particular freedoms and obligations will intentionally be set to be so different from that of legally recognized members. What then is deemed as a privilege exercised by the company can then not be similarly enjoyed by the members. The assets and properties of a company are set aside from that of members. Consequently, in case of a dispute arising from debt claims by any member, this can judicially be addressed separately. That is to say that the member who feels that the company owes him/her can only sue the company in a court of law and not any fellow member or any shareholder. This means that the company exists completely separated from that of its members.

The membership in a company can also be made up of members who are interested and those who are not interested. This implies that the members can include family members. In this respect, the listed members don't necessarily have to command a serious depth of influence or power to manipulate corporate decisions. This is a major milestone that the *Salomon's* case brought illuminated. A company can also have members who are not related and wield enormous power in the decisions of the day-to-day running of the company (Bonnici, 2013). It was also of great essence for any one dealing with any limited company to inspect the register of shareholders to ascertain and guarantee the desired value of their interests. This helps even creditors know the status of the company's financials that are of great effect in persuading suppliers and other stakeholders to know the extent to which they can do business with the company.

The Salmon's case has also elicited mixed reactions within legal, judicial, legislative and business circles, with calls to abolish private companies. This is so because it was deemed that private companies were taking advantage of legal loopholes to bypass liability as they make enormous profits. This will reduce the legal disputes that arise especially when a company is declared bankrupt leaving loans unpaid and creditors unsatisfied. This claim against private companies has led to rulings and judgments that contradict certain aspects of the Salomon's case.

Conclusion

The Salomon's case has helped building a great deal of jurisprudence and espoused the sorting out disputes even in small business. The safety of those involved in doing business with companies has also been reasonably and sufficiently enhanced. The company directors are also cushioned from unfair claims of compensation that otherwise would not have arisen if the company did not exist in the first place. These in-roads of company laws are so significant today even as high levels of mergers and acquisitions are witnessed. It will definitely help expose the business world in a state of anarchy and shrewd manipulations from malicious quarters in the business world. A company existing as a separate entity is automatically insured from the damaging missteps of individuals that are unjustified to interfere with its operations by law.

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