NOTE: 1. Open book exam - except students may not use materials borrowed from the UBC library.

THIS EXAMINATION CONSISTS OF THREE QUESTIONS
DO ALL 3.
You will recall that the facts of *Salomon v. Salomon & Co.*, [1897] A.C. 22 (H.L.), were set out by Lord Macnaghten as follows (at pp. 59-61 of the casebook, as you know):

Mr. Salomon ... was a wealthy man ... He was a boot and shoe manufacturer trading on his own sole account [and] 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. The eldest, who was about thirty years of age, was practically the manager. 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.

There was [an incorporation agreement and an incorporation application] ... registered, stating that the company was formed ..., and fixing the capital at £40,000 in 40,000 shares of £1 each. There were articles ... providing the usual machinery for conducting the business. The first directors ... were authorized 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 [original] subscribers ... 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
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transfer [of the assets of Mr. Salomon's business to the new company]. By an agreement dated August 2, 1892, the company [took over the business from Mr. Salomon]. The price fixed by the contract was duly paid. 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 £30,000 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 for the like amount. The balance, with the exception of about £1000 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 £1000 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, ...

The company had a brief career: it fell upon evil days. Shortly after it was 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 £5000, 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 realized 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.

The liquidator brought a claim against Mr. Salomon.

Assume that essentially the same facts recently occurred in B.C. and that the Salomons incorporated a B.C.A. company. Assume that both the liquidator and Salomon’s daughter (who we will assume has remained a shareholder) want to challenge what has occurred and make “somebody” in management liable. Assume - contrary to the actual facts - that everybody in the Salomon family still has substantial assets. What reasoned advice would you give the liquidator and the daughter? Be sure to indicate what further information you would need to give more precise advice.
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QUESTION 2

Marks 12

With reference to Question 1, if the Salomons had instead incorporated a C.B.C.A. corporation, how would your reasoned advice change?

QUESTION 3

Marks 35

Warren was severely injured a year ago in Big Okanagan City when he was run down by a taxi owned by Seon Cab Corp., a B.C.A. corporation, and negligently operated by Smith. Smith is the sole shareholder and director of 10 B.C.A. companies (including Seon Cab Corp.), each of which operates only two taxis. All ten companies use different phone numbers, but any call reaches the same line and a taxi of any of the ten companies might be despatched. Smith accepts calls on her personal phone line to send a cab, and, as is clear from the accident, she often drives one of the taxis personally if she cannot get one of her hired drivers to take the call. Smith has no contract with respect to such taxi operation, but she keeps the fare if she is driving. Some of the 10 companies are quite flush with assets, but not Seon Cab Corp. Smith is personally very wealthy. Assume that there are no taxi regulatory matters that affect this issue. Advise Warren.

END OF EXAMINATION