WILLIAM J. COMMON, *ès qualité* (PETITIONER)..... } APPELLANT;

AND

COLIN McARTHUR, (CONTESTANT).....RESPONDENT

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*Oct. 6, 7.

*Dec. 14.

ON APPEAL FROM THE COURT OF QUEEN'S BENCH FOR LOWER CANADA, APPEAL SIDE.

Joint stock company—Irregular organization—Subscription for shares—Withdrawal—Surrender—Forfeiture—Duty of directors—Powers—Cancellation of stock—"The Companies Act"—"The Winding-up Act"—Contributories—Pleading—Construction of statute.

After the issue of the order for the winding-up of a joint stock company incorporated under "The Companies Act," a shareholder cannot avoid his liability as a contributory by setting up defects or illegalities in the organization of the company; such grounds can be taken only upon direct proceedings at the instance of the Attorney General.

The powers given the directors of a joint stock company under the provisions of "The Companies Act" as to forfeiture of shares for non-payment of calls is intended to be exercised only when the circumstances of the shareholders render it expedient in the interests of the company and cannot be employed for the benefit of the shareholder.

APPEAL from the Court of Queen's Bench for Lower Canada (appeal side), (1) reversing the judgment of the Superior Court, district of Montreal, settling the list of contributories in the matter of The Dominion Cold Storage Company, in liquidation under "The Winding-up Act," and declaring the respondent to be liable as a contributory for the debts of the company, to the extent of the amount of $4,500 remaining unpaid in respect of his subscription for fifty shares in its capital stock.

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*PRESENT:—Sir Henry Strong C.J. and Gwynne, Sedgewick, King and Girouard JJ.

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A statement of the case will be found in the judgment reported.

Buchan and *R. C. Smith* for the appellant. Agreements made by a company to the effect of discharging shareholders from responsibility as regards its creditors are null and a fraud against both the creditors and other shareholders. Thomson on Corporations (ed. 1895) secs. 1511, 1514, 1517, 1550, 1579-1582, and cases there cited; Morawetz, Private Corporations, (2 ed.) secs. 302-309; *Spackman* v. *Evans* (1); *In re Agriculturist Cattle Ins. Co., Stanhope's Case* (2). See the, "Winding-up Act," secs. 41-49. The shareholder's liability for the unpaid balances on shares subscribed constitutes an asset of a company in liquidation, and such a liability brings the person liable within the meaning of the word "contributory." *In re Accidental and Marine Ins. Corp., Bridger's Case* (3); *In re Blakely Ordnance Co., Creykes's Case* (4).

The respondent cannot be permitted to usurp the functions of the Attorney General as to forfeiture of charter or to plead irregularities in the company's organization in order to avoid his liabilities as a shareholder.

The appellant submits that the respondent was rightly placed on the list of contributories, because the pretended cancellation of his subscription was a release to the detriment of creditors, was invalid, *ultra vires*, and did not discharge the respondent from his obligation as a shareholder; that even if the shares had been validly forfeited, he should still be placed on the list of contributories subject to the extent of his liability being determined when an order for payment is applied for.

(1) L. R. 3 H. L. 171.
(2) 1 Ch. App. 161.
(3) 4 Ch. App. 266.
(4) 5 Ch. App. 63.

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J. L. Morris Q.C. and *Béique Q.C.* for the respondent. The respondent ceased to be a shareholder when his shares were declared forfeited and taken over by the company. R. S. C. ch. 119, sec. 41.

The question is: Was the respondent liable as a contributor to the assets of the company at the time the winding up order was granted? There is no fraud or collusion complained of here and section 44 of the "Winding-up Act" does not apply to respondent, as he is not and was not a shareholder or member of the company when the company was put into liquidation. Sec. 45 applies only to shareholders who have transferred their shares under circumstances which by law do not free them from liability in respect thereof.

He could only have been held if he had retained his shares. The liquidator recognizes this and simply alleges that he is a shareholder. This being disproved his petition to fix respondent as a contributory, solely upon that ground, was rightly dismissed by the Court of Queen's Bench.

Sec. 41 of the Companies Act gives a right of action only to certain creditors of the company and not to the liquidator, and those creditors must first exhaust their remedies against the company under sec. 55.

The judgment of the court was delivered by:

SEDGEWICK J.—The Dominion Cold Storage Company was incorporated on the 28th of September, 1895, by Letters Patent, issued under the provisions of "The Companies Act" (Revised Statutes of Canada, chapter 119). In January, 1897, the company had become insolvent, and a winding-up order was made against it, the appellant William J. Common being appointed liquidator. On the 14th of June, 1897, he

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petitioned the Superior Court under the provisions of "The Winding-up Act" to settle the list of contributories, attaching to his petition a schedule in which appeared the names of all the persons whom he sought to hold liable as such contributories. In this list was the name of the present respondent, alleged to be liable in respect to fifty shares, the par value of which was five thousand dollars, and upon which five hundred dollars was credited.

The respondent, McArthur, contested his liability upon several grounds, the substantial ones being: First, that the Letters Patent incorporating the company had been obtained by false representations, and that the company had therefore never become legally organized; and secondly:

That on the second of October, 1895, the respondent wrote to said company stating that he withdrew his subscription, and requiring it to remove his name entirely from their books, and from that date he supposed his subscription was cancelled and withdrawn; that the formal minute of the said company cancelling his subscription was only entered upon their books on the sixteenth of November last (1896), but it should date back to and have effect from the second of October, 1895.

The first ground was disposed of before the Superior Court, it having been there held, and we think rightly, that it is not within the power of a shareholder, at all events after the winding-up order has been made, to set up defects and illegalities in the organization of a company incorporated under "The Companies Act," and that such a ground only can be taken by direct proceedings at the instance of the Attorney General. So that when the case came before us it was assumed that up to the second of October, 1895, he had been a shareholder of the company and then liable as a contributory for the amount unpaid on his subscribed shares. The only question now before us is whether under the circumstances presented in the evidence he

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had subsequently been released from that admitted liability.

The facts are undisputed. One Johnston was the principal shareholder and was the managing director of the company from the time of its organization until its collapse. To this gentleman Mr. McArthur, on the second of October, 1895, wrote the following letter:

DEAR MR. JOHNSTON,—Yesterday before I was out of bed I was served with a demand of assignment which was delivered in an uncovered form and caused no little excitement at No. 52. Then before 11 a.m., I had telephones from both "Bradstreets" and Dun & Co., and from Elliott an inquiry about 1 p.m. We were fortunate enough to keep it out of the papers.

When we called on Taylor he had not the money, and I had to give a cheque for $1,250, which prevented me from paying my clerks and travellers their salaries for the first time since I have been in business. In fact, had I not had this in bank for salaries, I don't know what we would have done. On inquiry this a.m., Mr. Gilman replied, "not sufficient funds in bank," and I had to send up our Mr. Brown to get it righted. To-day I was sent for by "Molsons," and after answering quite a lot of questions, I was informed that I must give up indorsing or signing notes for anything outside of the regular wall paper business or they would not have my account. So you see you must relieve me of all responsibility and take me off the "Cold Storage" altogether. I regret this very much, but at the same time cannot help feeling that both you and Mr. Taylor are very much to blame for it. Nothing else can be expected from doing business in such a hap-hazard way.

It is bad enough for yourselves, but to have me injured who has nothing to do with it is too bad. Taylor has the two notes still on hand, which had better be returned.

No reply having been received on the 4th of November he wrote another letter calling attention to the previous one. On the 12th of November he received the following reply:

Your letter of the 4th instant has remained unanswered and acknowledged until this date owing to my absence from the city till this morning. I now hasten to advise that, as a director, your name will not appear after to-day, but as a stockholder it will of necessity have to remain, the allotment having been made.

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I shall take the opportunity of seeing you before many days, and am glad to learn from Mr. McGregor that your health is improving.

It is in evidence that the company never made any demand upon the respondent for any portion of his unpaid stock. There is no evidence that any call was made upon any of the shareholders. It is certain, however, that no call was ever made upon him. But on the 16th of November, 1896, the directors passed the following resolution:

> Resolved: That whereas Colin McArthur, of Montreal, appears as a shareholder upon the books of the company for fifty shares of the stock of the said company of the par value of five thousand dollars (5,000.00), and whereas the said McArthur has failed and refused, after due notice, to meet the two calls, amounting to thirty per cent made on said stock, and has refused to acknowledge any liability on the same, therefore it was resolved to declare said shares forfeited under the powers provided for by by-law ten of the company, and that said McArthur should be considered to have withdrawn from the said company and to have forfeited all interest in said shares.

A perusal of the evidence leads to the inevitable conclusion that this resolution was passed at the instance of Johnston, not for the purpose of enabling the company to realize upon the stock as forfeited stock, but solely to release McArthur from his liability as a shareholder of the company in accordance with his written request made the year previously. The resolution was passed at a time when the company was hopelessly insolvent to the knowledge of the directors, and its only object could have been as I have stated. In the pleadings the respondent did not rely upon this resolution as a forfeiture of his shares but rather as an acceptance by the company of his surrender of them. He did not in his pleadings set out his non-liability by reason of the directors having declared them forfeited.

But in the present case it is immaterial whether the transaction in question be considered as a surrender or

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a forfeiture, inasmuch as neither the one nor the other would have the effect of releasing him from his liability. It is elementary law that a shareholder cannot, without statutory authority, surrender his shares to a company and thereby get rid of his liability as a shareholder. It is *ultra vires* of a company to so traffic in its own stock, unless its instrument of incorporation gives it the power, and it is not pretended that any such power existed here.

The only question is as to the effect of the alleged forfeiture. It is I think quite clear that there was in fact no forfeiture in the present case. The resolution was a collusive one, passed, not for the benefit of the company or its creditors, not for the purpose of enabling the directors to realise upon the forfeited stock, but for the purpose of conferring a benefit upon their friend McArthur. It was in fact the same as if the directors had taken from the treasury of the company the four thousand five hundred dollars due and had made a present of it to him.

The power of forfeiture given by the statute to the directors is given, not to be exercised for the benefit of the shareholders, but for the benefit of the company and its creditors. If a resolution like the one here had the effect of releasing McArthur from liability, similar resolutions might have been passed releasing all the other shareholders from liability, thereby destroying the capital of the company and absolutely defeating the claims of creditors. To contend for the legality of transactions that might lead to such consequences is in my view absurd.

Reference need only be made to the leading case of *Spackman* v. *Evans* (1) where it was held in effect that the power of forfeiture for non-payment of calls is a power that is intended to be exercised only when the

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circumstances of the shareholder render its exercise expedient in the interests of the company. It is not a power to be exercised for the benefit of the shareholder. The duty of the directors when a call is made is to compel every shareholder to pay to the company the amount due from him in respect of that call, and it is only when payment cannot be obtained that the power of forfeiture is to be resorted to. The power must be exercised *bonâ fide* for the good of the company, not to relieve a shareholder from liability.

Upon the authority of this case, we think that Mr. McArthur never ceased to be a shareholder of the company, and therefore, that he was properly placed upon the list of contributories.

If this view be correct we are not now called upon to express any opinion as to the liability of a person whose shares have been legally forfeited to be placed upon the list of contributories in respect of those shares.

How a person contingently liable to contribute to the debts of a company under winding-up proceedings is to be dealt with in the settling of [the list of contributories is a question which, so far as this court is concerned, remains open.

The appeal should be allowed with costs.

Appeal allowed with costs.

Solicitor for the appellant: *J. S. Buchan.*

Solicitors for the respondent: *Morris & Holt.*