

COMPANY LAW AMENDMENT COMMITTEE

Report

Of the

COMPANY LAW AMENDMENT COMMITTEE.

PRESENTED TO PARLIAMENT BY COMMAND OF HIS MAJESTY.

AT THE COUNCIL CHAMBER, WHITEHALL
This Twenty-seventh day of February, 1918.

PRESENT:

The Right Honourable Sir ALBERT HENRY STANLEY, M.P.

THE BOARD OF TRADE are pleased to appoint the following gentlemen, VIZ : -

The Rt. Hon. Lord WRENBURY (Chairman)

Mr. ARTHUR S. COMYNS CARR.
Sir FRANK CRISP, Bart.
Mr. GEORGE WELSH CURRIE, M.P.
Mr. FRANK GORE-BROWNE, K.C.
Mr. JAMES MARTIN.
The Hon. ALGERNON H. MILLS.
Mr. RICHARD DAVID MUIR.
Mr. CHRISTOPHER T. NEEDHAM, M.P.
Mr. HENRY A. PAYNE, C.B.
Sir OWEN PHILIPPS, K.C.M.G., M.P.
Sir WILLIAM PLENDER, G.B.E.
Mr. OWEN C. QUEKETT.
Mr. ANDREW WILSON TAIT.

to be a Committee to enquire what amendments are expedient in the Companies Acts 1908-17, particularly having regard to circumstances arising out of the War and of the developments likely to arise on its conclusion, and to report to the Board of Trade and to the Ministry of Reconstruction.

The Board are further pleased to appoint Mr. W. W. Coombs, M.B.E., to be Secretary to the Committee.

(Signed) A. H. STANLEY.

Mr. J. A. Torrens-Johnson was, on the 6th June, 1918, appointed an additional member of the Committee owing to the illness of Mr. O. C. Quekett.

REPORT OF THE COMMITTEE UPON THE AMENDMENT OF THE LAW UNDER THE COMPANIES ACTS, 1908 TO 1917.

To the Rt. Hon. Sir ALBERT H. STANLEY, M.P.,
President of the Board of Trade,

And to the Rt. Hon. C. ADDISON, M.D., M.P., Minister of Reconstruction.

1. On the 27th February, 1918, the Board of Trade were pleased to appoint a Committee "to enquire what amendments are expedient in the Companies Acts 1908 to 1917, particularly having regard to circumstances arising out of war and of the developments likely to arise on its conclusion, and to report to the Board of Trade and to the Ministry of Reconstruction." In accordance with the terms of our reference we have made a detailed enquiry into a number of questions which appeared to us relevant in this matter, and now report as follows:-

2. We issued in the first instance a number of questions to selected persons and bodies of persons competent to assist us in the matter. These included persons conversant with banking, commerce, law, shipping, accountancy, and the Stock Exchange. We received from them replies, all of which we have taken into consideration. Evidence has been given before us orally by 17 witnesses, whose names are given in the Schedule.

FOREIGN CAPITAL.

3. The question which lay in the forefront of our investigations and to which we attributed prime importance was that of the employment of foreign capital in British industries.

4. The preliminary question whether it is desirable that foreign capital should be freely attracted to this country is one upon which there was little, if any, difference of opinion. The maintenance of London as the financial centre of the world is of the first importance for the well-being of the Empire; anything

which would impede or restrict the free flow of capital to the United Kingdom would in itself be prejudicial to Imperial interests, and any legislation which would tend to impede or restrict the free flow of capital here by imposing restrictions or creating impediments ought to be jealously watched, lest in the endeavour to prevent what has come to be called "peaceful penetration" the normal course of commercial development should be arrested.

5. It is to be borne in mind that at the conclusion of the war-if it should be concluded upon such terms as we hope and anticipate-there is no probability that the countries which are now the enemies of the Allies will be those which will be in possession of capital looking for external employment. Outside the countries of the Allies it may be said, speaking generally and subject to exceptions of no great moment, that Europe will have little surplus capital to invest. The foreign capital which we have to contemplate will be capital flowing not from the Central Empires of Europe, but from other parts of the world, of which America may be the chief. To impose restrictions upon the influx of capital, aimed at our present enemies, with the result of deterring the flow of capital from (say) America, would be a policy highly injurious to the economic recovery and renewed prosperity of this country after the war. For these reasons we are of opinion that in all amendments of the law falling within the scope of our reference the expediency of the attraction of foreign capital should be steadily borne in mind, and anything which would have a restrictive or deterrent effect should, as far as possible, be avoided.

6. At the root of the whole matter with which we are here concerned lies a question which is not one of company law amendment at all, but one of high political and economic policy. The alien may come here to trade in any one of three characters. He may come as an individual; he may come in conjunction with others as a firm; or he may come in the form of a corporation. The fundamental question is whether in any one of these cases he ought or ought not to enjoy the same commercial freedom as the British subject British-born; and, further, whether, if some aliens ought to come freely, other aliens who are now our enemies ought to have the same facilities. It does not fall within our province to enquire whether the traditional policy of this country to admit and welcome all who seek our shores and submit themselves loyally to our laws ought, in the case of some and what aliens, to be revised; whether any and what restrictions ought to be imposed upon the alien who, in any one of these three characters, seeks to come here; or whether discrimination ought to be made between and alien of one nationality and an alien of another. That is a question of high political and economic policy which it is not for us to determine. The question of naturalised British subject as distinguished from British subject British-born is, again, beyond our sphere. We may probably assume that, as regards aliens generally, there is no intention to change the traditional policy of the country, and that we have to enquire whether-that being so-any amendment of the law of joint stock companies is expedient having regard to circumstances arising out of the war. But, as regards aliens who are now our enemies, it may be that the British Empire may adopt the policy that a special stigma ought to be attached to the German and that neither as an individual, nor as a firm, nor as a corporation ought he, for a time at any rate, to be admitted to commercial fellowship or to any fellowship with the civilised nations of the world. The existence of these questions has greatly increased the difficulty of our task, for until the policy is known, it is not possible to say how the Companies Acts should be amended to give effect to it. It has thus become necessary for us to indicate our conclusions in alternative form according as the policy adopted in these respects is one or another.

7. From the evidence before us and from deductions to be drawn from some recent legislation, we recognise that there exists (in some quarters at any rate) a desire-probably a strong desire-to ascertain and record the extent to which aliens are active in commerce here. The legislation to which we refer is such as: (1) the Registration of Business Names Act, 1916 (which, although originating as a projected measure long before the war, yet was pressed forward as a war measure because disclosure of nationality was, as a consequence of the war, made a prominent characteristic); (2) the Companies (Foreign Interests) Act, 1917, whose purpose was to prevent the elimination from articles of association of provisions restricting the amount of capital which might be held by aliens; (3) the Companies (Particulars as to Directors) Act, 1917, whose effect was, amongst other things, to enforce disclosure of the nationality of directors; (4) the British Ships (Transfer Restriction) Acts of 1915 and 1916, which rendered void any transfer not approved by the Board of Trade of any share of a ship or even any mortgage of a share of a ship to a person not qualified to own a British ship or to a "foreign controlled company"; and (5) the Non-Ferrous Metal Industry Act, 1918, which we shall have to consider further when we come to the case of companies engaged in "key

industries.” Of these Acts, Nos. (4) and (5) were limited in time with reference to the continuance of the war, but Nos. (1), (2) and (3) were not.

In April, 1916, the Committee appointed by the Board of Trade to investigate the general question of trade relations after the war reported against imposing restrictions upon aliens becoming shareholders in British corporations but in favour of “definite information as to the nationality of the shareholders in every British company.” The following is a quotation from paragraph (2) of the Report:--

“We think, therefore, that it would not be well to use the two-edged weapon of restriction, especially in view of the fact that after the war it will be unwise to discourage foreign capital from coming freely to this country. But we think it desirable that the Government should be provided with definite information as to the nationality of the shareholders in every British company. We therefore recommend that every limited company should henceforth be required to include in its annual return to Somerset House a statement of the amount of its stock or shares held by or on behalf of aliens, together with a statement of their nationality.”

The Committee, however, did not go on to state how the information as to nationality was to be secured.

On the other hand, Lord Balfour of Burleigh’s Committee in December, 1917 (*see* Cd. 9035, paragraph 154) discouraged any attempt to secure this information.

Many of those who have made written replies to our questions, or who have given evidence before us, have expressed opinions in favour of disclosure of nationality by all shareholders and in some cases of limitation of the proportion which aliens may hold of the share capital of a company. Others, on the contrary, are impressed with the mischief which may result from restrictions whose tendency will be to deter the influx of foreign capital. In the recommendations which follow in this report we have sought to bear steadily in mind the considerations on the one side and on the other to which we have directed attentions. We have not hesitated to express our own opinion as to the way in which, we have directed attention. We have not hesitated to express our own opinion as to the way in which, in our judgment, the balance falls, but inasmuch as it is for the Legislature to determine whether the policy of complete commercial freedom, or that of alien restriction generally, or alien restriction as regards certain aliens, is to be preferred we have indicated what in each of these alternatives are the amendments of the law of Joint Stock Companies which we think should be adopted.

ALIEN SHAREHOLDERS

8. If Foreign Capital is to be attached here it follows that, so far as such capital is invested in or utilised for the industries of Joint Stock Companies, it must be represented either by shares in such companies or by debentures representing indebtedness by them, and that its employment must be controlled by Boards of Directors appointed from time to time by the owners of the invested capital. The question, therefore, is whether restrictions ought to be imposed upon the extent to which the control of the company shall be allowed to reside in aliens, either by reason of their holding a majority of the shares, or of the debentures, or by reasons of their obtaining a majority upon the Board of Directors; and if so, how disclosure of their alien character is to be enforced.

9. Before dealing with this question it will be well to point out difficulties which present themselves in the way of securing disclosure of nationality and ensuring that aliens shall not command the control, assuming that it is desirable to prevent their doing so. The law of trusts is firmly established in this country. If A be the registered holder of a share, he is not necessarily the beneficial owner. He may be a trustee for B. To enact that the registered holder must be a British subject effects nothing. For B may be an alien and an enemy. Suppose, however, that you enact that A, when his share is allotted or transferred to him, shall make a declaration that he holds in his own right, or that he holds in trust for B, and that both A and B are British subjects. There is nothing to prevent the creation of a new trust the next day, under which C, an alien enemy, will be the person beneficially entitled. Further, at the earlier date (the date of allotment or transfer) the facts may be that A (a British subject) is trustee for B (a British subject), but that B (unknown to A) is a trustee for C, an alien enemy. The fact that B is trustee for C would be purposely withheld from A, and A’s declaration that he was simply trustee for B would be perfectly true. To require that A should make a declaration at short intervals (say once a month), or that A, B, C, and so on, should all make declarations would be, of course, so harassing and so detrimental as to be as matter of business

impossible. The only effectual way of dealing with the matter would be by a provision that the share might be forfeited, or might be sold and the proceeds paid to the owner, if an alien should be or become beneficially entitled to or interested in the share. Such a provision does not in the general case comment itself to us as practical or desirable.

10. Similar difficulties arise in any endeavour to control the nationality of the Board of Directors. It is easy, of course, to ensure that they shall all be, or that a majority of them shall be British subjects. But there is no means of ensuring that their action shall not be controlled by aliens whose nationality is not disclosed.

11. Having pointed out these difficulties, we approach next the question of policy. Bearing in mind the sources from which, as indicated above, foreign capital may after the War be expected to come:-

- I. Is it desirable to legislate in the direction of forbidding the employment of Foreign Capital here in Joint Stock Companies unless some such provisions as the following are satisfied:-
 - 1) That there shall be disclosure of the alien character of the foreign owner;
 - 2) That not more than a certain proportion of the company's shares shall be held by aliens;
 - 3) that the Board, or a certain proportion of the Board, shall not be alien; and
- II. Is it desirable to discriminate between one alien and another, and to legislate in that direction in the case of certain aliens and not of others?

In our answer to these questions we find it necessary to discriminate between different classes of companies, and we divide them into:-

Class A. – Companies generally not being companies within classes B and C.

Class B. – Companies owning British shipping; and

Class C. – Companies engaged in “key” industries

COMPANIES OF CLASS A.

12. In the case of companies generally (Class A) we recommend that no restrictions at all be imposed. We think that, bearing in mind the sources from which an inflow of capital is to be anticipated and encouraged, the balance is largely in favour of the absence of restriction, even although it involves non-disclosure of alien ownership. If there are restrictions, there must be disclosure of alienage, and the requirement of such disclosure might be thought to imply a stigma which in the case of our friends would be injurious. We have elaborated below a scheme of enforcing disclosure if that policy seems to the Legislature to be right. It is necessarily detailed and laborious: it puts difficulties in the way of investment in English securities, whether by British subject or alien. It would supply no doubt to the Board of Trade useful information as to the extent of foreign investment in English industries. But the price paid for the advantage would, we think, be too great. It is, after all, if adopted a scheme which can be evaded, and must to render it effectual be supported by consequences which should be imposed upon evasion. Simplicity and the absence of possible legal pitfalls are essential to free commercial development. We think the true policy is complete freedom so far as the law of Joint Stock Companies is concerned. Our recommendations go the length of allowing complete freedom as to the nationality both of the corporators and of the Board. They would allow, for instance, American capitalists to come here and establish themselves as a British corporation in which all the corporators and all the directors were American, and so of every other nationality.

13. We would make no discrimination, so far as the law of Joint Stock Companies is concerned, between aliens of different nationality. For if there is to be such discrimination there must be the machinery of disclosure, involving as we think a deterrent effect, acting prejudicially in the case of all investors. This is, however, a large national question which, as we have said, it is not for us to decide. If any such discrimination were adopted we think that at any rate it should be limited to some short period, say three or five years after the conclusion of the war.

Disclosure.

14. We turn next to the contingency that the Legislature may upon the question which it is not for us to determine consider that alien restriction is the policy to be preferred: that legislation should follow the lines which we trace in the recent statutes to which we have referred. In this case we submit the following scheme as a possible means of giving effect to that policy.

15. For reasons already given it is not possible efficiently to ensure full disclosure, but the following suggestions would, in the absence of deliberate and intentional evasion (which would be quite possible), meet the point and in the large majority of cases would disclose the extent of alien interests and control:-

- a) Every allottee of shares upon allotment and every transferee upon transfer should be required to make a declaration disclosing his nationality and whether he is the beneficial owner of the shares, and, if not, for whom he is trustee, and what is the nationality of the beneficial owner, and should undertake within a limited time, after any change in the beneficial ownership, to communicate the new facts to the company. In default of compliance with the above, the shares should, at the option of the company, either (1) be liable to sale by the company and the holder be entitled only to the proceeds; or (2) be liable to forfeiture and the holder entitled to receive payment from the company of ten per cent. less than the market value of the share, or, if there be no market value, then ten per cent. less than the value at which the share would be taken for *ad valorem* stamp duty if it were the subject of transfer. In case the company made default in exercising its power the Board of Trade should be authorised to require the above sale to be made.
- b) Every director, upon coming into office, should be required to make a declaration disclosing his nationality and stating whether in his office he is wholly free from the control or influence of any alien, and if he is not so free stating by whose directions or under whose control or influence he is to act and what is the nationality of that person, and should undertake within a limited time after any change in the state of things to communicate the facts to the Board and procure a statement of the facts to be entered in the Board Minutes. Any breach of these obligations to be visited with a penalty which should be severe.
- c) The company should be required to enter in the register of members, against the name of every registered member, his nationality as disclosed by the declaration. In the case where the registered member is not the beneficial owner, the company should be required to record, not in the register but in another book, the nationality of the beneficial owner as disclosed by the declaration, and, as regards the latter book, to record the nationality of any new beneficial owner when and as disclosed by the registered member. These particulars should be required to be included in the annual list under Section 26 of the Act of 1908. That list would thus become not a list of members only but a list of members with the addition of beneficial owners. The company should, further, be required to add to the annual list a summary of the result as regards nationality, showing (1) as regards registered members, how many are British subjects and how many shares they hold, and how many are aliens and how many shares they hold, sub-dividing the number of the aliens and their holdings under their respective nationalities; and (2) as regards the registered members who are British subjects: (a) how many of them are the beneficial owners and how many shares they hold; and (b) as regards the rest, what are the nationalities and holdings of the beneficial owners.
- d) The particulars as to directors to be introduced into the annual list by enlargement of the requirements of Section 26(l) of the Act of 1908.
- e) Existing shareholders should be brought in by the machinery presently suggested in paragraph 33.

16. The clauses should be so worded as that it should not be necessary to disclose mortgages of shares. It is true that this opens a door to evasion; but it is necessary not to interfere with commercial freedom in procuring loans upon shares.

[Note – The above recommendations do not cover the case of a company influenced or controlled in fact by its debenture holders. The existence of bearer debentures would make it impossible to extend the obligation of disclosure to debentures. We do not see our way to suggest the discontinuance of bearer debentures.]

17. If this or some similar scheme were adopted, it would form the basis of any principle which might be accepted as regards alien holdings, *e.g.*, that aliens (of certain nationalities) should not hold shares at all, or should not hold more than a certain proportion, or that aliens (of whatever nationalities) should not so

hold, or that the directors or a majority of the directors should not be of alien (or some defined alien) nationality, or under alien control.

18. We have already pointed out that any scheme of disclosure can be evaded by concealing the identity of the ultimate beneficial owner and, consequently, concealing his nationality. Further, if our recommendation of complete freedom and no enforcement of disclosure of nationality is adopted, it is, of course, *à fortiori*, possible that alien (possibly enemy) corporations may be established here. A suggestion has been made before us which we think it desirable to detail. It would, we think, cover the difficulties arising from both these points. Nevertheless, for reasons which we will assign, we do not recommend it for adoption. The case is supposed of a corporation British in form but alien in fact, whose alien nationality is effectually concealed and whose commercial activities are prejudicial to national interests. It is a corporation, let us suppose, which is using the advantages of British corporate life in a manner injurious to the national interests of this country. It may be seeking to control “key” industries; it may be seeking to injure British trade and to further unfairly the interests of the trade of another country by “dumping” its goods; it may be seeking to make “corners” to the injury of British and the furtherance of alien interest, and so on. There ought, it is said, to exist the means of stopping this. The suggested means is as follows:-

Establish a permanent commission framed something upon the model of the Railway Commission. The tribunal to consist of, say, five members, four commercial and one judicial – of whom the judicial member shall be president. The four members could either be permanent or selected from time to time from a panel. Give this tribunal jurisdiction to enquire *whether any corporation is by reason of the nationality of the corporators or of the persons interested in or carrying on or controlling the business of the corporation a company whose existence or commercial operations is or are for economic or political reasons injurious to the national interests of the British Empire or any part of the British Empire*, and if that be found to be the case to make an order to wind it up. The tribunal to be clothed with a very full discretion and to be entitled to act upon inferences reasonably drawn upon the principle that one of the parties before the Court knows all the real facts and has the means of displacing suspicion if suspicion arises, and that if he does not do so the Court is entitled to assume against him that suspicion based upon some reasonable grounds is well founded. The tribunal should be at liberty to infer who are the persons interested and what is their nationality from facts which justify an inference against them, although strict proof (which they could but do not supply) is wanting and the circumstances render it impossible for their adversary to give strict proof. The decision of the tribunal to be final and not subject to appeal.

19. If such a tribunal were constituted it would be essential to insure that it should not be capable of being used by one trader to injure the business of a rival trader (even though the rival be an alien) because rivalry in his business was injurious to his pocket. The words “for economic or political reasons” are intended to effect this. Further, it would be essential that access to the tribunal should be closely guarded as, for instance, that the right of application should be confined to the Attorney-General or any person interested who obtained the fiat of the Attorney-General.

20. But safeguard it how you will our opinion is that the existence of such a tribunal would so operate as a deterrent to the influx of foreign capital as that its possible utility in some future state of circumstances is not comparable as an advantage with the disadvantage which would result from the fact of its existence. Suppose that citizens of some foreign nation most friendly to Great Britain contemplated the establishment of a great industry in this country, they would naturally regard it as a possible contingency that friendly relations might unfortunately at some future time be disturbed, that “national interests” might require something at present unexpected but nevertheless possible, and that they might fall under the jurisdiction of this tribunal, and for this reason might abandon their project. We think that any such question had better be left to legislation which may be found to be appropriate when the particular case arises.

CLASS B.-COMPANIES OWNING BRITISH SHIPPING

21. The policy of the Merchant Shipping Act, 1894, as disclosed by ss. 1, 9 (v), 25, 28, 57, 69, 71 and 76, appears to be that British ships shall be owned only by natural-born British subjects or persons naturalized, &c., and although British Corporations are added by s. 1 (d), the inference is that the statute has overlooked the fact that a corporation, British by registration in this country, may in fact be alien in respect of the persons who are holders of or are beneficially interested in its shares. If the policy of the Act is such as we have stated it would in order to cover this point be necessary to amend the Act by adding

words at the end of Section 1, sub-section (d) so that it shall read "Bodies corporate established under and subject to the laws of some part of His Majesty's dominions and having their principal place of business in those dominions *and being bodies corporate of which all the incorporators and all the persons beneficially entitled to or interested in the shares of and interests in the corporation are persons falling within some one of the above sub-clauses (a), (b), and (c).*" The words added are printed in italics.

The result would be to leave naturalised British subjects and persons made denizens by letters of denization within the privileged class. This is a point with which we do not deal as we are not concerned with the general and large question of naturalization.

22. It will be observed that the above words hit the case of every person, however remote he may be from the registered shareholder in the corporation in question. If the shares are registered in the name of A, who is trustee for B, and B is a trustee for C, and so on, and if C or any subsequent letter of the alphabet is not a British subject the corporation in question could not, if those words were introduced, hold a share in a British ship.

23. The British Shipping (Transfer Restrictions) Acts, 1915 and 1916, adopt and enlarge the above policy and extend it to mortgages of shares in ships. These were excluded by s. 34 of the Act of 1894.

24. We have heard in evidence that individual ownership, as distinguished from corporate ownership, of British ships is, in the great shipping lines at any rate, now almost unknown. Ninety or even ninety-five per cent. of British ships we are told are now owned by corporations. The question of corporate ownership is, therefore, of great importance.

25. While we proceed to express the views which we have formed in the matter, we at the same time recognise that they may involve a departure from the policy of the Merchant Shipping Act. In this connection attention may be drawn to the recommendations in this matter contained in paragraphs 330, 331 of a recently published Report to the Board of Trade (Cd, 9092) of a Committee, appointed by Mr. Runciman on 27th March, 1916, consisting of shipowners and shipbuilders specially conversant with the subject.

26. We are satisfied upon evidence that the total exclusion of aliens from ownership of British ships is not essential for national safety and as a commercial matter is not expedient. A British line may be willing and desirous that its agent in a foreign port (being perhaps an alien) should have an interest in the success of the line. Or a British line may wish to make a working arrangement with, say, an American line under which each shall have, say, a one-fifth interest in the undertaking of the other. If the aggregate ownership by aliens does not confer more than 20 per cent. of the power of control they can neither carry an ordinary resolution nor defeat (much less carry) a special or extraordinary resolution. As regards the constitution of the Board, we are assured that 80 per cent. of the power of control can always secure the existence of a Board which will be representative of such nationality as that 80 per cent. approve. We therefore think that in these companies it would be sufficient to ensure that not more than 20 per cent. of the power of control should be in alien hands. We are not prepared to say that in this Class B there should be the same freedom as in Class A. We think that there should be this limit of 20 per cent.-that not more than 20 per cent. of the share capital should be held by aliens, and that those shares should carry no more than 20 per cent. of the voting power. Alternatively, we think, and indeed we should prefer, that the alien holdings should carry no vote at all-but that is a point of detail deserving further consideration.

1. It follows that in this Class B there must be disclosure of nationality and that allotment or transfer in breach of the limit should be forbidden and if made should be inoperative. Disclosure should be enforced in the manner detailed under the head of Class A in paragraph 15 of this Report, clauses (a), (b), (c), (d). Bearer shares must necessarily be forbidden.

2. Existing ownership in excess of the limit may, we think, be safely left undisturbed for the present.

3. An exemption from this legislation is necessary as regards certain ship owning corporations. There are corporations which own shipping as a subsidiary part of their undertaking, but which are not within the spirit of the veto which we seek to impose. Some of them are incorporated under the Companies Acts, others are not. The L. & N. W. Railway Company, the S.E. & C. Railway Company and other like undertakings own ships. Some gas companies and some commercial companies own colliers. Some of

these are companies incorporated under the Companies Acts. There is no intention of suggesting legislation which shall prevent, say, the L. & N.W. Railway from having alien shareholders beyond a certain limit. There should be legislation, therefore, to the effect that a corporation which owns shipping as a subsidiary and comparatively unimportant part of its undertaking may, with the licence of a defined authority, be taken out of Class B and put within Class A if its ownership of British shipping is confined within limits stated in the licence. The authority should be the same for all corporations whether under the Companies Acts or not – say, the Board of Trade.

[NOTE. – If our view in the above respects be adopted, the amendment above suggested in s. 1 of the Merchant Shipping Act, 1894, would not be made, but would be replaced by an amendment giving effect to the altered policy. This would be done by reference in the Shipping Act to the proposed new clauses in the Companies Act.]

CLASS C. COMPANIES CARRYING ON “KEY” INDUSTRIES.

27. We shall not attempt a definition of a “key” industry. The idea intended to be conveyed by the expression is fairly well known, and it would be possible by statute to define in general terms the characteristics of a “key” industry and then remit it to a defined authority, say the Board of Trade, to determine in each particular case whether the industry is a “key” industry. We shall assume that this is done and that the question is as to any amendments in Company Law expedient to deal with a company carrying of a “key” industry when the fact that it is carrying on a “key” industry has been established.

28. The typical case that has arisen is that dealt with by the Non-Ferrous Metal Industry Act, 1918. It may be thought expedient to leave any other case of key industry to be dealt with in like manner by an Act of Parliament *ad hoc*. But for our purpose we must assume that this is not so and that we have to say how it should be dealt with by general legislation amending the Companies Acts.

29. The question whether a company is one to carry on a “key” industry could seldom or never arise at the time of its registration. The modern memorandum of association includes such a multitude of objects that a “key” industry might be *intra vires* of almost any company. The question would arise when the company is carrying on business.

The Board of Trade we think should be empowered to make at any time an enquiry whether a company in Class A is carrying on a “key” industry or not, and if it finds that it is the company should fall out of Class A and into Class C, with the result that the following provisions shall apply:-

30. (a) The company shall, at the direction of the Board of Trade, by notice require every registered member to make a declaration such as under the disclosure procedure which we have suggested under Class A (*See* paragraph 15) he would have had to make if he were at the date of the notice about to receive an allotment or become a transferee, and in default the member shall be excluded from voting and receipt of dividend as in section 4 of the Non-Ferrous Metal Act.

(b) The company shall, at the direction of the Board of Trade, by notice require the holders of share warrants to bearer to surrender their warrants for cancellation and to have their names entered in the register and to make a similar declaration, and in default the share warrant holder shall be excluded from voting and receipt of dividend as above.

(c) All subsequent allottees and transferees shall be subject to the obligation of disclosure as suggested under Class A. (*See* paragraph 15.)

The above will ensure disclosure (subject, of course, to the possibility of evasion as before).

31. The limits of 20 per cent. recommended in the case of merchant shipping should then be made applicable, and if the 20 per cent. limit has in fact been exceeded the Board of Trade should be empowered to apply to the High Court for an order for sale of so much of the share capital as will reduce the alien holding within the limit with a direction that the Court shall so far as reasonably possible take the shares for sale rateably from the alien holders.

32. If companies of Class A were conceded the freedom which we recommend in paras, 12 and 13, it would be easy to devise machinery by which any particular company in that class could, if circumstances

rendered it desirable, be taken out of Class A and brought into Class C. We recommend that legislation should take that form.

INCORPORATION BY ALIENS.

33. The reasoning which leads to the conclusion that aliens should be allowed the freedom which we recommend leads also to the conclusion that it is not expedient to prevent or to seek to prevent aliens from incorporation companies in this country. They cannot, in fact, be efficiently prevented from so doing, for by obtaining the signature of British subjects to the memorandum of association they can achieve their object and the identity of those who stand behind the subscribers can, as above explained, be effectually concealed.

NAME OF THE COMPANY.

34. We have a further recommendation to make in the direction of disclosure. The name by which a company is called from many points of view a matter of no moment. But if a name be used which conveys a misrepresentation of the nationality of the company it may have a wide commercial effect. We think that there should be machinery for controlling the name employed so that a representation of nationality where the company is not British shall as far as possible be prevented. For this purpose we recommend that:-

- a) When application is made for registration of a new company and the name suggested states or conveys expressly or by implication British nationality the Registrar may require to be satisfied upon the question of nationality and may refuse to accept the name unless the articles of association contain clauses providing to the satisfaction of the Registrar or of the Board of Trade that the new company will in fact be British. This would apply not only when the word British or some similar word forms part of the name, but to all cases in which an implication of British nationality arises which in the opinion of the Registrar would be liable to mislead. The question whether the proposed name is liable to mislead or not should be left largely to the discretion of the Registrar. For the question whether a name will mislead or not is necessarily matter of opinion.
- b) When an existing company is trading under a name which states or conveys expressly or, in the opinion of the Registrar, by implication British nationality and the Registrar is satisfied that the nationality is not British, he may (subject to a right in the company to apply to the Court) call upon the company to change its name to an approved name, and if within a limited time the company fails to do so the Registrar may (subject to the like right) by order under his hand change the name to such name as he approves, and that name shall thenceforward and until some further authorised alteration of name be the statutory name of the company.

[NOTE.- There are cases in which the Registrar has already assumed that he has a power of control over such words as "Royal" or "Imperial." If legislation such as we suggest is adopted, it should be so expressed as to give the Registrar a discretion in that class of case.]

35. Considerable discretion should be left to the Registrar, for it is not every case in which a name conveyed by implication that the company was British in which it would be right to interfere.

BEARER SHARES.

36. Disclosure and bearer shares are mutually inconsistent. If a policy of disclosure is adopted bearer shares must go.

If, however, disclosure be negated the opinion of those whose evidence we have received as to the expediency of bearer shares is divided. The balance is in favour of retaining them. By British investors they are not largely held, but British investors seem to be inclining towards them. To the foreign investors (including the American investor), they seem to appeal strongly. They attract the small Continental investor, and reach him through his local bank, which is probably a branch of or in correspondence with a London bank. The system is such as the following:- A bank domiciled in London has branches in many places abroad or has correspondents who are local bankers in places abroad. The foreign local bank is in touch with the small investor, who is perhaps interested in a particular industry such as carried on by the British company which issues the bearer shares. Share warrants in the company are taken up by or for the

small investors; they are all, in fact, placed in the control and probably in the possession of the bank in London. The result is that that bank is for all practical purposes the undisclosed member of the company in respect of the aggregate amount of the foreign holdings and is in a position to exercise the voting power. We think that bearer shares should be maintained. We have not gathered any sufficient reason for abolishing them, and the reasons in their favour are weighty. If control should become necessary the machinery would be supplied by the insertion of provisions that the company may and upon notice from the Board of Trade shall call in the share warrants for cancellation and their right to vote and to receive dividends shall be suspended until the share warrant has been superseded by registration.

FRESH ISSUES COMMITTEE.

37. In answer to a question whether after the war some restriction should be imposed upon the issue of capital similar to that now exercised by the Fresh Issues Committee at the Treasury we have received replies almost without exception in the negative. Such restrictions would be quite out of keeping with the freedom which we think desirable.

We pass now to questions not directly arising out of the war or of the developments likely to arise on its conclusion.

ISSUE OF SHARES AT A DISCOUNT - ASSESSMENT OF SHARES.

38. More than a quarter of a century ago Lord Macnaghten, in *Ooregum Company v. Roper*, 1892, A.C. 145, speaking of the Companies Act, said: "The dominant and cardinal principle of these Acts is that the investor shall purchase immunity from liability beyond a certain limit on the terms that there shall be and remain a liability up to that limit." The principle thus stated is quite clear, and had it been adhered to many difficulties which are now well nigh insuperable would not have arisen. The legislature has, and the Courts have – if it be not a contradiction in terms – adhered to the principle but not maintained it. The development of the law has allowed payment to be made upon shares by the transfer of property which need not be shown to be in value the pecuniary equivalent of the amount due upon the shares. Payment of commission to a person in consideration of his subscribing for shares or procuring subscriptions for shares has been allowed by Statute. But it has never in so many words been provided that the allottee of a £10 share may satisfy all liability upon the share by paying, say, £1. Neither has the Legislature said in so many words that after the £10 has been paid the company may return it or part of it to the shareholder except by the statutory proceedings for reduction of capital.

39. The question we have to consider arises when the law stands in the above illogical and indefinite form. It is of the following nature: - A company has been formed with a capital of, say, £100,000 in £10 shares. Assume that they have all been taken up and all paid in full, in cash, but that £50,000 of the cash has been lost and the market value of the fully-paid share is, say, £5. The company wants more capital, but obviously in that state of facts cannot obtain subscribers for new £10 shares on the terms that they shall pay £10. Two courses may be possible if the law allowed them:-

- a) The company could obtain subscribers for new £10 shares upon the terms that upon payment of £5 there should be no further liability. This would be an issue at 50 per cent. discount.
- b) If the company could impose on the existing holder of a £10 share that he should be liable for a further £5 per share on his £10 share, with the alternative that if he would not accept that liability he should be valued out and lose his share, receiving payment of such sum, if any, as would be attributable to his share if the company were wound up, then the company might be able to obtain a new subscriber for a £10 share on the terms that he should pay £10 for it. This would be a case of assessment upon the existing shareholder.

40. Each is a case in which new terms are imposed upon the existing shareholder against his will. His bargain was to contribute £10 to a common stock: to risk its employment in a defined trade until the will of the statutory majority of the shareholders or the intervention of the Court at the instance of shareholders or creditors stopped the trade: and to take his chance of profit from that employment. He was never to pay any more and the adventure was to continue until the money was all lost or the undertaking was stopped by a winding up. If any new adventurers came in they were to come in on the statutory terms of liability up to the nominal amount of the share. Is it desirable to alter the law? The question is one of expediency.

41. The evidence before us leads to the conclusion that it is desirable to alter the law. But if that course is adopted it is necessary to consider another matter. If shares are to be allowed to be issued at a discount so that the full nominal capital will never be received ought payment of dividends out of capital still to be forbidden so that the full nominal capital will ever be received ought payment of dividends out of capital still to be forbidden so that the amount in fact received in respect of capital must be maintained intact except so far as it is dissipated by loss?

And yet another question – If the course proposed is adopted ought the present statutory scheme for reduction of capital to be varied and how?

Taking these several questions in order we are of opinion as follows:-

42. ISSUES OF SHARES AT A DISCOUNT.- The original principle as stated in Lord Macnaghten's words has been already so infringed that it cannot be said to continue to exist as a cardinal principle. The evidence before us is that commercially the issue of shares at a discount is desirable. There is we agree no principle in this. It is a concession to commercial experience. Principle, however, has as instanced above already been abandoned, and issue of shares at a discount is but accepting in practice that which has already been conceded in fact by allowing payment of commission in consideration of a person subscribing for shares.

43. At the same time we think that the amount of discount should be so controlled as that the provisions of the Act in respect of capital shall not be illusory. There should be a statutory limit to the discount allowable, and if the disease is so deep-rooted as that the statutory limit is not sufficient for the purpose the matter should be left to winding up. For these purposes the issue of shares at a discount should be controlled as follows. It should not be allowed at the beginning or at the earlier stages of a company's career. It should be allowed only when the company's issued share capital is at a discount, and a maximum percentage of discount should be fixed. We recommend that five years after commencement of business shall be the earliest date for issue, and that the price shall not be lower than five per cent. below the market value of the similar existing shares in issue if there be a market price, or five per cent. below the price at which the existing shares would upon transfer be taken for *ad valorem* stamp duty under the Stamp Act if there is no market price, and that the discount shall never exceed 50 per cent. Thus, if the £10 share stood in the market at £6 the price should not be lower than £5 14s., that is to say the discount should not exceed £4 6s., and in no case should the discount exceed £5. Further there should be ample provision for complete publicity. The balance sheet, the annual statement, and every prospectus should state in plain terms the discount which has been given. Section 89 of the Act of 1908 should be so amended as to exclude commission payable to a person in consideration of his subscribing for shares and to confine the word "commission" to meaning either brokerage which is a payment made for services rendered or underwriting commission which is a payment made for a guarantee given.

44. ASSESSMENT.- The object which is sought to be attained by assessment is now attained by what is called reconstruction. Reconstruction is a proceeding by which the company is put into liquidation and the assets are sold to a new company formed for the purpose with a share capital so arranged as that such of the shareholders as assent take shares in the new company with a further liability, and those who do not are paid off in liquidation. The objections to this mode of procedure are principally first that it is very expensive and secondly that a winding up always creates commercially a certain amount of prejudice. The expense arises principally from the fact that new revenue duties have to be paid exactly as in the case of a new company, although in fact the transaction really consists in rejuvenating an old one; and that a very large amount of clerical work is involved. If issue of shares at a discount is to be allowed we see no objection to allowing assessment. It sins against the original principle in a manner which is the converse to that in issue of shares at a discount. The latter allows a reduction, the former allows an increase in the amount which according to the original principle of limited liability was to be the member's limit of liability. As matters stand assessment is but achieving in another and a cheaper form that which can be done already.

45. For the protection of the minority of shareholders, however, we recommend that there shall be the following restrictions. A power to assess shares should not be allowed to be included in the memorandum or articles of association of the company either originally or by alteration of the articles. An assessment should only be made under the authority of a special resolution approving the particular assessment

proposed. It should further be provided that every special resolution must mention a sum per share to be paid in cash to such members as dissent and that the dissentient member shall be entitled at his option either to accept that sum or to demand an arbitration to determine what sum shall be paid with a further provision that there shall be only one arbitration and in that arbitration the dissentients shall appear together, but with power to any dissentient to appear separately at his own expense, or if the arbitrator shall order at the expense of the company. The costs of the arbitration to be borne as the arbitrator shall direct.

REDUCTION OF CAPITAL AND PAYMENT OF DIVIDENDS OUT OF CAPITAL.

46. In the above paragraphs 44 to 47 we have gone as far as we think it expedient to go. The law as to reduction of capital and as to payment of dividends out of capital should, we think, be maintained at present.

47. Opinions have been expressed before us in favour of a principle which would abandon altogether the nominal amount of a share in a company limited by shares, and would even allow registration of a company with shares carrying no liability. The idea is that the company might sell a share in its undertaking for such sum as an interest in the company might command and that its capital fund should consist exclusively of the aggregate sum obtained by the sale of such interests as a share represents. This they contend is but the logical outcome of the condition to which the law has come by allowing issue of paid-up shares against property not of value equivalent to the nominal amount of the shares—commission for subscribing for shares—and issue of shares at a discount (if issue at a discount should now be openly allowed). They further advocate the allowance of payment of dividends out of capital, safeguarded only by provisions which would allow of the recall of capital so distributed if within a limit of time the money were required for payment of debts.

48. Your Committee are not prepared to accept any such radical alteration of the law. The present basis of limited liability in a company limited by shares is that the liability of the member is to be limited to the amount if any unpaid on his shares. (See section 2 of the Act of 1908.) If the member is to be under no liability or the amount paid on his shares is not to constitute and to be retained (subject only to loss incurred) as capital, the law must be made to rest not upon any amendment of the existing Acts but upon legislation starting from a different point of departure and proceeding upon wholly different lines.

49. In the recommendations which we have made in this Report we have gone as far in the direction of meeting the views above indicated as we think it possible to go if the fundamental principle of the present law is to be observed at all. And, as we have already stated, we should not have been prepared to go so far but for the fact that the original principle of the Act of 1862 has already been so largely ignored as that a further concession to commercial opinions will probably do no harm and would in fact only openly permit that which under the law as it at present stands can in fact be achieved.

MEMORANDUM OF ASSOCIATION.

50. The Companies Acts require that the memorandum of association of a company shall state “the objects of the company.” It was laid down more than forty years ago in *Ashbury Railway Carriage Company v. Riche*, L.R. 7, H.L. 653, that the memorandum of association is the company’s charter and defines the limitation of its activities and the destination of its capital. It is perhaps not matter of surprise that under these circumstances commercial men looked to see whether in the memorandum of association were to be found words justifying the particular commercial transaction into which they contemplated entering. But in so doing they forgot that that which the Act required the memorandum to state was “the objects of the company,” and not the powers by the exercise of which those objects were to be attained. For instance, the object of the company might be to open and carry on an hotel at Dover. To achieve that object the company must have power to hold land to erect a building, to buy furniture, to employ a staff of servants, and so on. But none of these were objects. They might and probably would further want to borrow money, giving very likely a mortgage on the property. But borrowing was not their “object”; it was an act which they would do if they could in order to achieve their object, viz., to run their hotel as a commercial success. However, an evil practice grew up of crowding into the memorandum of association words that would cover every conceivable act which the corporation could under any circumstances desire to do. Objects were buried and concealed in an accumulated mass of powers. The resulting mischief was twofold. The intending investor who ought to have been informed with reasonable clearness as to what

was the trade in which his money was to be risked could often learn nothing except that his money might be used for any conceivable purpose. And the intending creditor was deprived of the advantage of knowing what his intending debtor could and could not do in the employment of its capital.

51. This abuse reached its climax in the case of the Anglo Cuban Company, recently argued in the House of Lords under the name of *Cotman v. Brougham*. The memorandum of association of the company there in question after 30 paragraphs of the widest kind, very few of which defined objects at all, concluded with a clause to the effect that the objects set forth in any paragraph should not be restricted by the terms of any other paragraph and that none of the paragraphs or the objects specified in them should be deemed subsidiary or auxiliary to the objects mentioned in the first paragraph. Having regard to the provision in section 17 of the Act of 1908 that the Registrar's certificate of incorporation is conclusive evidence that all requirements of the Act in respect of registration and of matters precedent and incidental thereto have been complied with and that the association is a company authorised to be registered and duly registered under the Act, the House of Lords was compelled to assume that this was a memorandum of association which stated "the objects of the company."

52. We recommend that the Act be amended by providing that the memorandum of association must state the objects but must not state the powers of the company, that such powers of the company as it is thought necessary to state shall be stated in the articles, and that there should be introduced into the Act a section providing that every company shall have certain powers as detailed in the section except in so far as the articles of association exclude them. The power of borrowing of subscribing for shares in other companies of purchasing other businesses and a number of similar and other powers would then find their proper place and the memorandum of association would be reduced to its proper function in defining the trade of the company or other the object which it is to pursue with a view to earning profit.

REGISTRAR'S CERTIFICATE.

53. As the law at present stands the Registrar's certificate is conclusive upon the matters mentioned in Section 17. This throws a very heavy burden of responsibility upon an official who has neither the time nor the means of being satisfied upon all the matters on which his action is to be conclusive. It is certainly of the first importance that when the company is about to contract engagements there should be no room for doubt whether it is a corporation or not. But we think the Act goes too far. If the requirements of the Act have not in fact been complied with; if (say) the association was not one authorised to be registered under the Act; if the so-called memorandum of association is not a memorandum of association such as the Act requires there ought to exist the means of questioning this provided that it can be done with justice to those who have dealt with the body as a corporate body. This can be achieved if the body be treated as a corporate body during its existence, but that existence can be brought to an end upon the ground that it never ought to have begun. We recommend that it shall be a ground for winding up a company that the requirements of the Act in respect of registration or of matters precedent or incidental thereto have not been complied with or that it was not an association authorised to be registered under the Act, and that upon that application the Registrar's certificate shall not be evidence conclusive or at all. Lord Davey's Committee by para. 16 of their report in June, 1895 (C. 7779), recommended a clause making it a cause of winding up that a certificate of incorporation has been obtained by fraud, misrepresentation or mistake, or by a wilful violation of any provision of the Companies Acts. And they added to it a recommendation that there should be cause for winding up if the Court is satisfied that the company was formed or that its business has been carried on with the intent or in such manner as to defraud, defeat or delay the creditors of the company or of any other company or person, or for any fraudulent or illegal purpose. With these recommendations we agree.

54. While it should be a ground for winding up that the requirements of the Act have not been complied with it should be left to the discretion of the Court to make or to refuse a winding up order on that ground according as it is or is not just and equitable that an order should be made. If, for instance, the defect does not go to the root of the matter or if the business and the position of the company are such as that it ought to be allowed to go on, or if creditors would be prejudicially affected by a winding up, the Court should have power to refuse an order and (if it thinks fit) to give validity to the invalid registration.

AUDIT AND AUDITORS' CERTIFICATE.

55. We have made enquiry into the question whether the law should be amended by requiring that the auditors must have some and what professional qualification. We do not make any recommendation to that effect. We have not traced any mischief which requires remedy in the matter.

56. Section 113 of the Act of 1908 requires that the auditors shall report whether the balance sheet "is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs according to the best of their information and the explanations given to them and as shown by the books of the company." We have made enquiry whether the words "and as shown by the books of the company" should be omitted and the certificate should be that the balance sheet exhibits "a true and correct view of the state of the company's affairs." We are without hesitation of opinion that it would be highly inexpedient indeed, we may say impossible, to require a certificate in that form. The decisions in *London and General Bank* (No. 2), 1895, 2 Ch. 673, and *Kingston Cotton Mill Co.*, 1896, 1 Ch. 331, 2 Ch. 279 have delimited with great distinctness the extent and limits of the auditor's responsibility. We do not think they can reasonably or profitably be extended.

DISCLOSURE OF PROFIT AND LOSS.

57. Section 26 (3) of the Act of 1908 provides that the annual summary required of every company other than a private company must include a statement in the form of a balance sheet, but the balance sheet need not include a statement of profit and loss. We have made enquiry whether a profit and loss account ought to be included. We do not recommend that it be required. As a commercial matter publication of profit and loss ought not to be required in the absence of very strong reason, and we do not find that such reason exists. To require from a corporation a public disclosure of profit and loss which is not required from a firm or an individual, gives an unfair advantage to a competitor in trade and does not commend itself to our judgment. But we think that it may reasonably and without public mischief be required that the statement in the form of a balance sheet to be included in the annual summary shall state the amounts or rates of dividend which have been paid since the last balance sheet or are proposed for payment as the result of the trading. And we recommend an amendment of the law to that effect.

PAYMENT TO DIRECTORS FREE OF INCOME TAX.

58. We have learned that there exists a practice in some companies of making the payments to directors *quà* directors free of income tax, including supertax. Assume that a director's fees are to be £100 a year free of income tax and supertax. The additional sum which he in fact is paid by reason of his being relieved of income tax is a sum not fixed but varying according to what his aggregate income from all sources may be. The rate demandable from him for income tax may be 6*s.* in the pound or may be some less sum. Further (and this is the mischief at which we point in particular) the supertax of which he is relieved may vary in a very much larger degree. If his aggregate income is small there may be no supertax demandable at all. If it be large the supertax may be 4*s.* 6*d.* in the pound. The payments which the directors receive should be of an amount openly stated and plainly known without any necessity of computation to every member of the company. The sums payable to directors are in some cases large, so that the additional sum due to relief at the expense of the company from income tax and supertax may be substantial. The shareholders ought to know what the directors' remuneration is. We recommend that payment to directors free of income tax or of supertax shall be forbidden.

DISTINGUISHING NUMBERS OF SHARES.

59. Section 22 of the Act of 1908 requires that each share shall be distinguished by its appropriate number. The present system of denoting numbers attached to shares creates a very large amount of clerical work. Shares of very small nominal amount – not infrequently as low as a shilling, and very frequently as low as £1 – are now common and this is true of very large concerns. The preparation and checking of transfers and the records in the company's books in such cases involve a large amount of clerical work. We have been pressed in evidence by gentlemen who represented the Institute of Secretaries to recommend that upon these grounds the distinguishing numbers of shares shall be abandoned. We are not satisfied that as regards fully paid shares-or even as regards partly paid shares-the distinguishing numbers are essential for any useful purpose. But we find that the Committee of the Stock Exchange and some of the Banks wish

to retain them (although others do not), while the Chambers of Commerce are divided in opinion. On the whole we do not in this state of opinion recommend that distinguishing numbers be abandoned.

PRIVATE COMPANIES.

60. We have ascertained from the Board of Trade that (approximately not exactly) the total number of companies on the register is 66,000 and of these no less than 50,000 are private companies. These figures show and the evidence before us has shown that the private company has met a want. The principal attraction of the private company lies in the fact that the company need not make the annual statement required by Section 26 of the Act of 1908. It avoids the necessity of an annual publication of facts from which the success or failure of its trading may be ascertained. The private company might no doubt be used for purposes of fraud, but there is no evidence before us that it is so used. It has been on its trial for about 10 years. We think it has up to the present justified its existence and should be left undisturbed.

GENERAL OBSERVATIONS.

61. In addition to the several matters upon which we have above submitted observations and recommendations a number of other matters have been the subject of evidence before us and have been considered and discussed by the Committee.

Evidence has been given before us upon such subjects as whether a company should be restricted in respect of borrowing, whether floating charges upon all present and future assets should be allowed, whether the requirements of the Act as regards prospectuses are sufficiently exacting, whether those requirements should be extended to foreign companies, whether a vendor to the company should be allowed to take shares or debentures in payment, and if he takes shares whether he should be precluded from selling them for some and what time, whether promoters in the form of corporate bodies should be allowed, whether investigation at the public expense of the affairs of a company where there is reason to suspect fraud ought to be facilitated, whether incorporation by registration should be deferred until some defined amount of capital shall have been subscribed and paid up in cash. Most of these were exhaustively considered by Lord Davey's Committee in 1895. Upon none of these do we find that any sufficient grievance or mischief exists to call for any alteration at the present time of the existing law. Some are already controlled and much better controlled by regulations of the Stock Exchange than they could be by legislation. One which was tried in the form of provisional registration was after experience abandoned in 1856, and Lord Davey's Committee reported against it in June, 1895 (*see* para. 24 of their Report, C. 7779).

We have received from several sources, such as (1) a memorandum from the Registrar of Joint Stock Companies; (2) suggestions from the Official Receiver in Companies Liquidation, and (3) correspondence from persons and bodies conversant with and interested in the branch of the law with which we have to do, numerous suggestions as to points, some of minor others of greater importance, in which it is said that the Companies Acts might with advantage be amended.

62. We have considered that it is not within the spirit of the reference under which we are sitting to deal with matters such as these, or at any rate, that we ought not to delay this report in order to investigate them. Our primary duty we have taken to be to enquire and report as to amendments expedient having regard to circumstances arising out of the war and of the developments likely to arise on its conclusion. We have given these words-prefaced as they are by the word "particularly"-a liberal interpretation, and have gone into some matters which appeared to us of importance sufficient to justify our including them. But we have not thought it right to go into a general enquiry as to amendments in the law which do not bear upon the exceptional state of circumstances with which we are asked to deal.

63. We desire to express our appreciation of the zeal and ability shown by Mr. W. Walter Coombs in the discharge of his duties as Secretary to the Committee.

We have the honour to be
Your obedient Servants,

WRENBUIRY.
A. S. COMYNS CARR.

JAMES MARTIN.
ALGERNON H. MILLS.

OWEN PHILIPPS.
WILLIAM PLENDER.

FRANK CRISP.
G. W. CURRIE.
F. GORE BROWNE.

RICHD. D. MUIR.
C. T. NEEDHAM.
H. A. PAYNE.

A. W. TAIT.
J. A. TORRENS-JOHNSON.

W. WALTER COOMBS,

Secretary.

July 15th, 1918

Mr. Torrens-Johnson dissociates himself from the recommendation that companies should be empowered to issue shares at a discount, and he has signed the foregoing report subject to that reservation.

NAME OF THE WITNESSES WHO HAVE GIVEN EVIDENCE.

LORD FARINGDON.
Mr. CLAUSON, K.C.
Mr. FREDK. WHINNEY.
LORD CUNLIFFE.
Mr. ERNEST COOPER.
The Rt. Hon. F. HUTH JACKSON.
Mr. A. W. FLUX
Mr. HAROLD BROWN.
Mr. H. E. BURGESS.

Mr. W. WATKINS.
Mr. W. H. STENTTFORD.
Mr. R. A. PINSENT.
Mr. J. W. BUDD
Sir ALFRED A. BOOTH, Bart.
The Hon. Mr. Justice YOUNGER.
Sir JOHN R. ELLERMAN, Bart.
Mr. S. E. CASH.

RESERVATION BY MR. A. S. COMYNS CARR.

It is with particular regret that I find myself unable to sign the Report without adding the following reservations. This is especially so in view of the fact that I have been unavoidably prevented from attending a considerable number of the meetings of the Committee. I have, however, carefully considered the evidence which has been given and the replies received to the questionnaire issued by the Committee, and while in agreement with the greater part of the Report, and in particular with the recommendation that no steps should in general be taken to control the holding of shares by aliens, I consider it my duty to express my dissent from the following conclusions:-

1. Those relating to companies owning British shipping (paragraphs 21-29 inclusive).

The main question seems to me to be whether the experience of peace and war has shown that on balance this country has lost or gained more by permitting ships to be registered as British ships when they are owned by a company which has alien shareholders. It is to be noted that it is not usually a question of permitting a ship which would in any case be British to be under the control of aliens; the question is whether, if a number of persons, some or all of whom are aliens, own a ship, they should be permitted to register it as a British ship by forming themselves into a British company and establishing an office in the British Dominions. If they were not permitted to do so they would still own the ship, but register it as a foreign ship in some other country. It appears that a number of ships were registered here before the war by companies with alien shareholders (some even with enemy shareholders). They were (as the Committee were informed by a very distinguished representative of the shipping world) managed in this country; the profits earned by them were subject to our taxation; they were obliged to conform to the regulations of our Merchant Shipping Acts; they carried officers and men who were members of the Royal Naval Reserve; on the outbreak of war our Government was able to requisition the ships owing to their British registration and without regard to the nationality of the shareholders in the companies owning them.

It appears to me that all of these consequences have been highly advantageous to this country, and that none of them would have ensued if British registration had been refused to the ships in question. I have not been able to gather from the evidence on the subject (which shows considerable divergence of opinion) what are the disadvantages alleged on the other side. In any case in which the management has been suspect it has been open to the authorities during the war to supersede it by that of official controllers, if they did not wish to adopt the simpler and more efficacious remedy of requisitioning the ships. It is true that as the Merchant Shipping Acts now stand it was, until the passing of the British Ships (Transfer Restriction) Acts, 1915 and 1916, possible at any moment for the owners of a British ship to dispose of it

and remove it from the register; it may be that it would be wise to alter this in future, and to require at least a substantial notice before the removal of a ship from the register; but in any case the position can be no worse than it would have been if the ship had never been on the register.

For these reasons I am unable to concur in the recommendation of my colleagues.

2. Those relating to Key Industries (paragraphs 30-35 inclusive).

For similar reasons I am unable to concur in these recommendations. Again it appears to me that the important thing is to get the industries established in this country, and that the question of their ownership is of secondary consequence. In many cases, industries of the kind rather vaguely described as "Key industries" are the subject of patents which may be taken out by aliens; the policy of the Patents and Designs Act, 1907, is to compel such patentees to manufacture the patented article in this country; these recommendations seem to me to be in conflict with that policy, of which I approve. Further, if aliens are not permitted to own such industries here, they will merely establish them elsewhere, and it by no means follows that any British subject will establish them here. In any case these recommendations would not prevent aliens from carrying on the same industries in this country as individuals or firms or by means of companies registered abroad. If restrictions are desired (which I deprecate) it seems to me that they would have to be imposed by a system of licensing similar to that adopted in the Non-Ferrous Metal Industry Act, 1918.

3. Those relating to disclosure (paragraphs 15 and 16).

While agreeing that any system of enforcing disclosure of the nationality of shareholders must be cumbrous, and only partially effective, I would suggest that if any is adopted it should be confined to the element of control-*i.e.*, it might be enacted that no voting power should attach to a share and no remedy be available in respect of a debenture, unless there had been lodged with the company (or filed with the Registrar) a reasonable time previously and confirmed at the time, declarations by the registered holder, and if he is a trustee, by the person or persons (or, in case any of them is a minor, his parent or guardian) claiming to be for the time being the ultimate beneficial owners, giving such particulars as may be required. As long as a declaration is furnished by some person who swears that he is the ultimate beneficial owners, intermediate trustees can (it seems to me) be ignored, and the risk of evasion is confined to the case where that person is prepared to commit deliberate perjury. This method would not interfere with bearer shares, nor with the free transfer of any securities, since the declaration would only be required as a condition of voting or otherwise exercising a right of control, and not as a condition of ownership. There may be certain advantages in knowing who are the real controlling parties in a company, apart altogether from the question of nationality.

4. General Observations (paragraphs 64 and 65).

I cannot agree that the subjects dismissed in these two paragraphs were unworthy of the attention of the Committee. They are concerned mainly with the better prevention of various methods of company promotion and management which have involved the investing public in serious losses in the past. This appears to me to have a very special importance "having regard to circumstances arising out of the war and to the developments likely to arise on its conclusion." We have seen during the war a remarkably widespread diffusion of money, and a wonderful growth in the habit of investment, among classes of the population to whom both are a novelty. It is computed that no less than 13,000,000 people are directly interested in various forms of Government war securities. After the war be expected that a large number of people who never were investors before will be willing to entrust their savings to commercial companies, but will not be very well equipped to select those which are worthy of their confidence. Simultaneously there will be a large crop of new schemes appealing for public support, mostly *bonà fide*, but offering unique opportunity to the fraudulent and over-sanguine. In my opinion it would be a disaster if by such means the money of the new class of investors were to be lost, and they were ultimately to be frightened away.

As the majority of the Committee have abstained from dealing with these questions, I can hardly go into them in detail, and will only say that in my view the radical defect of our present system is that we allow companies to be registered, prospectuses to be issued, shares to be allotted, practically without check (except in mere formalities), and it is only after the harm is done and the money spent (often years after),

that in a small proportion of the worst cases there follows official investigation and, in a still smaller proportion, punishment. In my view prevention is better than cure, and the right line of reform is to permit no prospectus or other appeal for funds to be issued in this country by any company, British or foreign, or by any person desiring to call attention to the merits of any company in order to dispose of its shares, unless a copy of the document is filed with the Registrar, and he is satisfied (not, of course, as to the truth of the statements contained in it) but that it does contain in a prominent position a plain answer to all questions on which the law requires disclosure, and unless there is also filed with him a statutory declaration by every director that he has investigated the statements and is satisfied of their truth. Further, no allotment should be permitted until the subscriptions are sufficient to provide, over and above any sums to be paid to vendors and promoters, a sum stated in the prospectus to constitute in the opinion of the directors adequate working capital. With these and other reforms (as to which valuable material exists in the information collected by the Committee) I am of opinion that the risk of the misfortunes which I have indicated might be greatly minimised.

A. S. COMYNS CARR

July 15th, 1918

The Committee find it necessary to state the circumstances under which Mr. Comyns Carr has signed a minority report. He was present at two preliminary meetings on March 14 and April 23. At the next eleven meetings he was not present at all. These were the meetings at which the Committee heard the evidence and, upon its completion discussed all the materials before them, arrived at their conclusions and recommendations, and on June 11 adjourned for report. On June 25 and July 2 they settled the draft report- Mr. Carr was present for a short time on June 25. He did not attend the meeting on July 2.

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JAMES MARTIN.

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