Friday, July 3.

SECOND DIVISION.

[Lord Kincairney, Ordinary.

MACFARLANE, STRANG, & COMPANY, LIMITED *v.* BANK OF SCOTLAND.

Fraud—Company—Promotion of Company—Bank—Flotation of Bogus Company by Bank to Secure Payment of Overdraft—Action by Creditor of Limited Company against Bank—Verbal Statement by Bank as to Credit.

A firm of ironfounders raised an action against a bank for payment of £8297, in which they averred that they had a contract to supply cast-iron pipes to J. Y. & Sons, a firm of public works contractors; that before any of the pipes were delivered J. Y. & Sons had, unknown to the pursuers, but to the knowledge of the defenders, become hopelessly insolvent, and owed £27,000 to the defenders, of which sum the defenders were unable to obtain payment; that the defenders thereupon entered into a fraudulent arrangement with J. Y. & Co. to float the firm as a limited company with the intention (which was successful) of securing payment of the defenders' unsecured overdraft out of the moneys obtained from the public for the preference shares of the company, and the proceeds of the goods supplied by manufacturers and merchants to the company; that the defenders acted as bankers to the company and revised the prospectus, which contained misrepresentations as to the assets of the company, and that the company was a bogus and fraudulent concern floated by the defenders for their own purposes; that the company requested the pursuers to make delivery to them of the pipes ordered by J. Y. & Co., whose contracts the company had adopted; that the defenders, in pursuance of their fraudulent scheme, reported verbally to the pursuers' bankers, on their inquiring at the pursuers' request, that the company was good enough as a business transaction for the sum named, between £1000 and £2000; that the pursuers thereupon delivered cast-iron pipes to the company to the value of the amount sued for, that the goods so delivered were never paid for, the firm of J. Y. & Co. being sequestrated and the limited company going into liquidation within six months of the flotation, and that the pursuers' loss was due to the fraudulent actings of the bank.

Held that the action was irrelevant.

Question whether the pursuers' averments as to the bank's actings in the flotation of the company would have been relevant if made in an action brought against the bank by a shareholder of the limited company.

On 30th April 1902 Macfarlane, Strang, & Company, Limited, ironfounders, Lochburn Ironworks, Glasgow, raised an action against the Governor and Company of the Bank of Scotland for £8297, 2s. 11d., with interest from the date of citation till payment.

The pursuers averred—"(Cond. 2) In the month of April 1898 pursuers received an order from James Young & Sons, railway and public works contractors, Bryson Road, Edinburgh, for cast-iron pipes. . . . Although the contract was made in April 1898 no part of it was executed and no pipes had been delivered by the pursuers up to 10th March 1899. (Cond. 3) By the beginning of 1899 the business of James Young & Sons . . . had become hopelessly insolvent. Amongst the large liabilities of the firm was an unsecured overdraft with the defenders' bank to the extent of over £27,000, for payment of which the defenders had long been pressing without success. In the month of January 1899 the defenders, knowing the whole circumstances of the firm, refused further assistance, and definitely demanded payment of the overdraft. Negotiations thereupon took place between Mr Robert Young, the sole partner of the said firm, Mr John L. Kerr, contractor, Leith, and Arthur Drummond, C.A., Edinburgh, or one or more of them, on behalf of the said firm of James Young & Sons, and the treasurer of the bank Mr George Anderson, and the cashier thereof Mr John Bisset, or one or other of them, acting for and on behalf of the defenders, as a result of which the fraudulent scheme and device after mentioned was entered upon and carried through by them, under which money was to be obtained from the public and goods from manufacturers and merchants so as to enable the business to be carried on during the period of public subscription, both the public and merchants being wilfully kept ignorant of the true state of the business. It was accordingly determined to convert the business of James Young & Sons into a limited liability company with the object of obtaining from the public funds wherewith to meet the firm's liabilities, and especially the overdraft due to the defenders. (Cond. 4) Accordingly, on or about the 1st of March 1899 there was issued the prospectus of a company to take over the business of James Young & Sons. The company was incorporated on 2nd March 1899 under the name of James Young & Sons, Limited. The capital of the company was £100,000 divided into 5000 5 per cent. cumulative preference shares of £10 each and 5000 ordinary shares of £10 each, and the price payable to the vendors, who were the firm of James Young & Sons and Mr Robert Young, then the sole partner of said firm, for the business, with the whole assets thereof, as set forth in the prospectus, was as follows:—(1) 5000 ordinary shares of £10 each, being the whole ordinary shares, and (2) £50,000 in cash, representing altogether £100,000. . . . The said prospectus was issued with the full knowledge and approval of the defenders, who, through the said Mr George Anderson and Mr John Bisset, or one or other of them, were

consulted from time to time during the formation of the company, and were kept fully informed of all the negotiations and arrangements in connection therewith, and the draft of the prospectus was submitted to and revised by the defenders. The statements in the prospectus were, and were known to the defenders to be, *inter alia*, untrue in the following respects:—(The pursuers specified various statements relating to the assets to be acquired by the company from the vendors, amounting, as stated in the prospectus, to £100,072. The pursuers averred that the company had not acquired these assets, and also that some of them were subject to rights in security. (Cond. 5) The subscription list for the preference shares of the company opened on Monday, 6th March, and closed on Wednesday, 8th March. On the latter date all the directors of the company then acting signed at the request of the defenders, and delivered to them, a letter undertaking not to proceed to allotment without the consent of the defenders unless the shares were fully applied for, and not to pay any portion of the proceeds thereof to the vendors without the consent of the defenders. The shares were not fully applied for. The number of preference shares actually applied for by the public was 3390, and the total amount received from the public therefor was £31,539. This amount was not sufficient to ensure a quotation of the shares of the company on the Stock Exchange. Accordingly on 9th March the defenders agreed to grant to the directors of the company as individuals (except Mr Douglas Westland, who was abroad), along with Mr John Martin, assistant secretary of the North British Railway Company, an overdraft of £10,000, the directors and Mr Martin agreeing to apply for and assign to the nominees of the defenders preference shares to that amount, and at the same time to apply the price of said shares in reduction of James Young & Sons' overdraft, said sum to be held to be in part payment of the cash consideration payable by the company to the vendors. Certain arrangements were also made as to further security for repayment of this new overdraft, and it was also stipulated and the directors undertook that the balance of the overdraft of the old firm should be paid in cash out of the proceeds of the shares taken up by the public to the extent of not less than one-half of said proceeds. (Cond. 6) On 9th March a meeting also took place between the said Mr George Anderson and Mr John Bisset, or one or other of them, acting on behalf of the defenders, and the secretary of the company, the said Arthur Drummond, and in consequence of the arrangement come to at that meeting the directors of James Young & Sons, Limited, proceeded to allotment, and 1000 preference shares were allotted to themselves along with Mr Martin. These shares were afterwards assigned to two of defenders' officials by transfer dated 23rd March 1899, which transfer was registered on 30th May following. These shares were paid for by a cheque drawn on the new overdraft account mentioned in the preceding article, which cheque was duly credited to the company. The company at the same time gave a cheque for £10,000 to the vendors, who paid it into the overdraft account of the old firm of James Young & Sons with the defenders towards the reduction of said overdraft. In accordance with the arrangement mentioned in the previous article the defenders also received out of the proceeds of the preference shares of the company taken by the general public large payments to account of the overdraft of the old firm. . . . While the money subscribed by the public was thus, under the scheme arranged as aforesaid, being received from the public, it was being impounded by the defenders for the payment of long-standing debts due to them, and in the knowledge and as part of the scheme of the defenders the company was thus being rendered practically helpless, and without any capital available for carrying on the business for which it was ostensibly floated. (Cond. 7) The said limited company was floated by and at the instance of the defenders, who acted throughout by their treasurer, the said George Anderson, and their cashier, the said John Bisset, in order that they might save, or at all events reduce, the loss which they were bound to make through having granted to the firm of James Young & Sons without security the large cash advances above mentioned. Prior to the flotation of the company the firm of James Young & Sons was in the knowledge of the defenders hopelessly insolvent, and must soon have become notour bankrupt. But for the pecuniary assistance given by the defenders the flotation of the company could never have taken place. By the flotation of the new company the defenders intended to secure and succeeded in securing payment of their large unsecured overdraft or of the greater portion thereof out of the moneys obtained from the public for the preference shares of the company, and the proceeds of the goods supplied by manufacturers and merchants to the company. (Cond. 8) . . . The company on its formation adopted the current contracts of the old firm with various traders, and among the contracts so adopted was that of the pursuers. On the 10th March 1899 the company . . . requested the pursuers to begin delivery of the pipes, &c., ordered from them by the old firm. (Cond. 9) The pursuers accordingly began on 15th March 1899 to make delivery of the pipes, &c., in question, and continued doing so until 14th July 1899. . . . At the end of the first month's deliveries the pursuers requested payment in terms of the contract, but the company, in place of paying cash as contracted for, asked the pursuers to accept their bill for the amount of the month's deliveries. The pursuers, . . . in view of the prospectus, . . . took the company's bill for the amount and passed it on to their bankers (the British Linen Company Bank), requesting them to inquire and report regarding the position of the company. The British Linen Company Bank made inquiry accord-

ingly at the defenders' head office in Edinburgh, and communicated to the pursuers the report they had received from the defenders, which was that the company was good enough as a business transaction for the sum named, between £1000 and £2000. This report was in the knowledge of defenders and of the said George Anderson and John Bisset entirely untrue, and was made by them in pursuance of the fraudulent scheme by which they were combining with the firm of James Young & Sons or the parties before named on its behalf to obtain goods and credit for the concern, and keep it afloat until they had received payment of their overdraft as aforesaid. The pursuers, believing this report, continued to supply goods to the company and retained the company's bill, and also took their acceptances for part of the goods, which they subsequently delivered to the company. The first bill, which was dated 12th April 1899, had a currency of three months, and on its becoming due on 15th July 1899 it was dishonoured. The pursuers thereupon immediately stopped further delivery of goods to the company. (Cond. 10) The value of the goods supplied by the pursuers to the company, together with the bank charges on the several bills, all of which were dishonoured and had to be met by pursuers, is £8297, 2s. 11d. The estates of James Young & Sons were sequestrated on 11th August 1899, and James Young & Sons, Limited, went into liquidation on 15th September 1899. . . . The pursuers understand that the trustee on James Young & Sons' estate claims the whole assets of the limited company on the ground that there never was any delivery or proper transfer of the assets from the firm to the company, and that the company failed to carry out its part of the agreement between them. In any event only a very small dividend can be paid to the creditors of the limited company. The pursuers therefore cannot hope to recover from the company, and have suffered loss to the extent of the sum sued for. (Cond. 11) But for the formation of the limited company at the instigation and with the active assistance of the defenders as aforesaid for the purposes of the fraudulent scheme above condescended on, the firm of James Young & Sons would have speedily become bankrupt, and no deliveries of goods would ever have been made to them by the pursuers. Further, had they been aware of the true nature of the company, and of the fact that practically the whole share capital subscribed was being appropriated by the defenders in payment of the indebtedness of James Young & Sons to them, the pursuers would never have consented to the company taking over their contract with the old firm, but would have refused to transact with the company, or to assist it in any way, either by deliveries of goods or otherwise. The said company was in reality a bogus and fraudulent concern, floated by the defenders for their own purposes, as above narrated, and was never solvent at any time. The loss sustained by the pursuers is the consequence of the fraudulent scheme promoted by the defenders, and of their actings and representations in the carrying out of the same."

The pursuers pleaded—"(1) The pursuers having suffered loss and damage to the amount concluded for through the fraudulent actings of the defenders and their treasurer and cashier, or one or other of them, as above condescended on, are entitled to decree therefor, with expenses, (2) The said company having been formed, and the pursuers' goods having been obtained, in pursuance of the fraudulent scheme condescended on, decree should be pronounced as concluded for."

The defenders pleaded, *inter alia*—"(1) The pursuers' statements are irrelevant and insufficient to support the conclusions of the summons."

On 14th February 1903 the Lord Ordinary (KINCAIRNEY) pronounced the following interlocutor:—"Finds that the averments in the condescendence for the pursuers are irrelevant: Therefore dismisses the action, and decerns: Finds the defenders entitled to expenses," &c.

Opinion.—"This is, in my opinion, a difficult case. It is also a singular case; indeed, so far as I have been informed or know, quite unprecedented. There is no authority for it. It is not an action on contract or for breach of contract. It is rested expressly on allegations and pleas of fraud on the part of the bank, but it is not rested on any misrepresentations said to have been made to the pursuers. The bank has pleaded that it is irrelevant, and after careful consideration I have come to be of that opinion. The action is of this nature. The pursuers, Macfarlane, Strang, & Company, Limited, ironfounders, had, or say they had, a contract with James Young & Sons, contractors, to furnish them with iron pipes; the contract was made in 1898, but for some reason not explained no pipes were delivered until 10th March 1899. Before that date, and on 2nd March 1899, the company of James Young & Sons, Limited, was formed professedly for the purpose of acquiring, carrying on, and extending the business of James Young & Sons, and was incorporated; and it adopted, among other current contracts of the firm, the contract with the pursuers, the implement of which had not then been commenced. Thereafter the pursuers, in fulfilment of their contract, made deliveries of iron pipes until 14th July 1899 to the value, as the pursuers allege, of £8297, 2s. 11d. A bill of theirs was then dishonoured, and the estates of James Young & Sons were sequestrated on 11th August 1899, and James Young & Sons, Limited, went into liquidation on 15th September 1899. The causes of the failure of the firm and company are not stated. The pursuers say that the trustee on James Young & Sons' estate claims the whole assets of the limited company, on the ground that they were never effectually transferred from the firm to the company, and that the company will pay only a very small dividend to its creditors.

"In these circumstances the pursuers endeavour by this action to recover their

loss, or rather the loss which they apprehend, from the Bank of Scotland. What has been said discloses no ground of action against the Bank of Scotland, the defenders, but there is an averment in condescendence 9 that the Bank of Scotland gave to the pursuers' bank a favourable opinion of the financial position of the company, which was untrue. But the pursuers admitted in argument that they could not found on this opinion, in respect of section 6 of the Mercantile Law Amendment Act, because it was not in writing. That condescendence is therefore to be held as out of the case.

"The pursuers aver in condescendence 4 that the prospectus of the limited company was untrue in certain particulars detailed. But it does not appear to me that there is any relevant averment of error in the prospectus, because it is not said in the prospectus that the company had acquired the leases or the contracts referred to, but only that they were held by the firm of James Young & Sons, and would be made over to the limited company. Further, it is not averred that the pursuers ever saw the prospectus, at all events not until a late date, or were misled by it or induced by it to deliver pipes to the limited company. Further, I consider that even if the pursuers had seen the prospectus, and if it was untrue, and if they had been misled, no action on that ground could have been sustained, except at the instance of an allottee, consistently with the judgment in *Peek* v. *Gurney*, 1873, 6 E. and I. Appeals, 377. Had the pursuers been allottees, it may be that they might have maintained a case against the bank as promoters, in virtue of the Act 53 and 54 Vict. cap. 65. But they are not in a position to plead that Act.

"But the pursuers' case is really not rested either on the opinion expressed by the bank on the inquiry of the pursuers' bankers, or on any criticism which may be made on the prospectus. I have no doubt that they could not succeed on either of these grounds.

"But if I rightly understood the pursuers' argument, they put their case quite differently; and it would be the same whatever the prospectus was. The pursuers say that James Young & Sons owed the bank £27,000, which is true; that the bank were unable to enforce payment of it, which may be probable; and that Young & Sons were on the verge of bankruptcy, which is not admitted and not explained; and they aver that the limited company was formed with the object of obtaining from the public subscribing and paying for shares, as much money as would pay the debt to the bank; that according to the prospectus £50,000 was payable to the vendors, that is to James Young & Sons, in cash, which would be available for payment of the debt due to the bank; that the bank revised the prospectus; that when the subscriptions were insufficient to secure a quotation on the Stock Exchange the bank granted the directors a draft for £10,000 which enabled them to complete the subscription; and I understand it to be averred that sufficient money was obtained from the public subscribing to enable the directors to pay either the whole of the £50,000 payable as cash to the vendors, or enough of it to enable the vendors to pay their debt to the bank, and that the bank did receive from the vendors the whole or the greater part of their debt.

"The pursuers make the averment that the bank 'floated' the company. But that is a loose averment made in inexact language, to which I can attach no meaning, and which I must disregard. So far as I can see, the only things which the bank are said to have done are these—they are said to have revised the prospectus, their name appears on it as the bankers of the company, and they advanced £10,000 on the personal security of the directors; and I do not see that it is averred that they did anything else.

"I find it very difficult to say from these averments what is the exact ground of action against the bank. It is fraud, no doubt, but not misrepresentation or concealment.

"I do not find it averred or pleaded that the limited company were the agents of the bank, or the bank of the company. It is nowhere averred that the bank carried on the business of railway contractors through the agency of the limited company, and I do not think that I ought to consider such a case until it is averred or pleaded.

"The case is laid on fraud alone, and, as I have said, fraud without misrepresentation.

"It is said that the design was to obtain money from the public wrongfully. The persons wronged, if such a design were put in operation, would be the public from whom the money would be obtained, that is to say, the allottees, but certainly not persons who merely traded with the company. It is clear that everyone who traded with the company, and in the course of such trading became creditor of the company, would have as good a claim against the bank as the pursuers have. But such a liability is unknown unless in the case of principal and agent.

"The pursuers say that the company was a bogus company. But a general averment of that kind can receive no effect unless the meaning of it is explained, and I do not see how the facts support it at all.

"The assets of the firm are stated in the prospectus. They are said to be of the value of above £100,000, and much more than the half of this is said to consist of the value of buildings and plant. It is not said that no such buildings or plant existed or that they were overvalued, and I do not see how it is possible to designate a company to which such assets are transferred as a bogus company. It is not averred that it did not carry on business.

"It is not very easy to see in what the loss of the pursuers consisted. It was incurred in carrying out a contract with the firm of James Young & Sons, and had no limited company ever been formed the pursuers would apparently have lost the same amount had they carried out the con-

tract with the firm. They choose to say that that would not have happened, because James Young & Sons would have immediately become bankrupt, and the deliveries would have ceased. But that appears to be *gratis dictum*, and is an averment of too general and haphazard a character to be accepted as relevant. Anything might have happened. The bank, for example, might have supported the firm without incurring any liability for doing so. The pursuers further say that if they had known that the money subscribed to the company was to be employed in payment of the debt of the bank they would not have transferred their contract with the firm to the limited company. But it does not appear that they had any right to know the manner in which the company employed its funds. The pursuers cited no case at all parallel to this or lending it any support; and on the whole I am unable to say that the pursuers have relevantly averred that they were misled by the bank into giving credit to the company or that they suffered any damage by the formation of it. I am therefore of opinion that the defenders must be assoilzied."

The pursuers reclaimed, and argued—The case was relevant. It was quite distinct from *J. & S. Paton* v. *The Clydesdale Bank, Limited*, October 23, 1895, 23 R. 38, 33 S.L.R. 22; *rev.* May 12, 1896, 23 R. (H.L.) 22, 33 S.L.R. 533. That action was held irrelevant because the pursuers did not aver a case of fraud by means of a combination to which the bank was a party. Here there was a distinct averment that the bank entered into a fraudulent combination to float a fictitious company with the result of loss and damage to the pursuers. The misrepresentation made by the defenders as to the financial position of James Young & Sons, Limited, could be proved as part of the fraudulent scheme, although the statement was not in writing.

Counsel for the defenders were not called upon.

LORD TRAYNER—I agree with the Lord Ordinary in thinking this to be a singular case. The pursuers seek to make the defenders liable for a debt due to them by Young & Sons, although the defenders had no connection whatever with the incurring of that debt nor guaranteed its payment. The case presented by the pursuers is that Young & Sons being debtors to the defenders, and being in the knowledge of the defenders hopelessly insolvent, the defenders adopted the course—or aided and abetted it—of forming Young & Sons into a limited company, in which the public were invited to take shares, in order that out of the money subscribed by the public they might operate payment of their debt. This (according to the pursuers) the defenders did, well knowing that the limited company had no assets, and that the public were invited to buy shares which had no value. In short, the pursuers' case is, that the defenders swindled the public, or aided in doing so, in order to obtain payment of the money due to them by Young & Sons. I assume that statement to be true, as on a question of relevancy, although I am far from attributing to the defenders any such misconduct. But assuming the pursuers' statement, I think it not relevant to support the conclusions of the summons. The pursuers took no shares in the limited company, and therefore lost nothing by the defenders' actings. The averments of the pursuers, if made by an allottee of shares might present some relevancy, but in support of the pursuers' claim they appear to me altogether irrelevant. The mode in which the pursuers seek to connect their loss with the defenders' alleged proceedings is this—they say that the floating of the limited company gave it a fictitious credit, and that if the defenders had not floated the company they (the pursuers) would not have given it credit as they did. But if they gave undue credit to the limited company, that was their own fault. They should have made sure of the sufficiency of the company before giving it credit. The defenders are not liable because the pursuers gave large credit to their customers before satisfying themselves that they were safe in doing so. I agree with the Lord Ordinary that the action should be dismissed.

LORD MONCREIFF—I am of the same opinion. I sympathise with the opening sentences of the Lord Ordinary's opinion, in which he describes the singularity of the present action. The explanation is simply that the action is hopelessly irrelevant.

The LORD JUSTICE-CLERK concurred.

LORD YOUNG was absent.

The Court adhered.

Counsel for the Pursuers and Reclaimers—Shaw, K.C.—Hunter—Wark. Agents—J. & J. Galletly, S.S.C.

Counsel for the Defenders and Respondents—Clyde, K.C.—Cullen. Agents—Tods, Murray, & Jamieson, W.S.

Saturday, July 4.

FIRST DIVISION.

[Sheriff-Substitute at Glasgow.

SNEDDEN *v.* JAMES NIMMO & COMPANY, LIMITED.

Reparation—Negligence—Duty to Public—Children—Child Falling into Ditch by which Waste Boiling Water Discharged.

In an action of damages against a colliery company for the death of a child of four the pursuer set forth that the child had been killed by falling into a ditch through which waste water at a high temperature was discharged from the boilers at the defenders' colliery. The ditch was situated by the side of a piece of waste ground between the col-